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TITLE 7—AGRICULTURE

Chapter I—Agricultural Marketing Service (Standards, Inspections, Marketing Practices), Department of Agriculture

PART 51—FRESH FRUITS, VEGETABLES AND OTHER PRODUCTS (INSPECTION, CERTIFICATION AND STANDARDS)

SUBPART—UNITED STATES STANDARDS FOR FLORIDA TANGERINES [1]

On June 30, 1955, a notice of proposed rule making was published in the FEDERAL REGISTER (20 F. R. 4650) regarding a proposed revision of the United States Standards for Florida Tangerines.

After consideration of all relevant matters presented, including the proposal set forth in the aforesaid notice, the following United States Standards for Florida Tangerines are hereby promulgated pursuant to the authority contained in the Agricultural Marketing Act of 1946 (60 Stat. 1087 et seq., 7 U. S. C. 1621 et seq.).

GRADES

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51.1810 U. S. Fancy.
51.1811 U. S. No. 1.
51.1812 U. S. No. 1 Bronze.
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AUTHORITY: §§ 51.1810 to 51.1836 issued under sec. 205, 60 Stat. 1090, 7 U. S. C. 1624.

GRADES

§ 51.1810 *U. S. Fancy.* "U. S. Fancy" consists of tangerines which are mature, firm, and well formed, and which are free from soft bruises, bird pecks, unhealed skin-breaks, and decay and free from damage caused by ammoniation, creasing, dryness or mushy condition, green spots or oil spots, pitting, scale, sprouting, sprayburn, sunburn, unsightly discoloration, buckskin, melanose, scars, scab, dirt or other foreign materials, disease, insects, or mechanical or other means.

(a) Each fruit in this grade shall be highly colored.

(b) In this grade not more than one-tenth of the fruit surface, in the aggregate, may have a light shade of brown discoloration caused by rust mite, or an equivalent of this amount in appearance when the fruit is discolored by any cause. (See § 51.1819.)

§ 51.1811 *U. S. No. 1.* "U. S. No. 1" consists of tangerines which are mature, firm, and well formed, and which are free from soft bruises, bird pecks, unhealed skin-breaks, and decay, and free from damage caused by ammoniation, creasing, dryness or mushy condition, green spots or oil spots, pitting, scale, sprouting, sprayburn, sunburn, unsightly discoloration, buckskin, melanose, scars, scab, dirt or other foreign materials, disease, insects, or mechanical or other means.

(a) Each fruit in this grade shall be fairly well colored.

(b) In this grade not more than one-third of the fruit surface, in the aggregate, may have a light shade of brown discoloration caused by rust mite, or an equivalent of this amount in appearance when the fruit is discolored by any cause. (See § 51.1819.)

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[1] Packing of the product in conformity with the requirements of these standards shall not excuse failure to comply with the provisions of the Federal Food, Drug, and Cosmetic Act.

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A numerical list of the parts of the Code of Federal Regulations affected by documents published in this issue. Proposed rules, as opposed to final actions, are identified as such.

CODIFICATION GUIDE—Con.

§ 51.1812 *U S. No. 1 Bronze.* The requirements for this grade are the same as for U. S. No. 1 except for discoloration. In this grade at least 75 percent, by count, of the fruits shall show some discoloration, and more than 20 percent, by count, of the fruits shall have more than one-third of their surface affected with bronzed russeting: *Provided,* That no discoloration that exceeds the amount allowed in the U. S. No. 1 grade shall be permitted unless such discoloration is caused by thrip, wind scars, or rust mite. (See § 51.1819.)

§ 51.1813 *U S. No. 1 Russet.* The requirements for this grade are the same as for U. S. No. 1 except for discoloration. In this grade at least 75 percent, by count, of the fruits shall show some discoloration, and more than 20 percent, by count, of the fruits shall have more than one-third of their surface affected with discoloration. (See § 51.1819.)

§ 51.1814 *U. S. No. 2.* "U. S. No. 2" consists of tangerines which are mature, fairly firm, and fairly well formed, and which are free from soft bruises, bird pecks, unhealed skin-breaks, and decay, and free from serious damage caused by ammoniation, creasing, dryness or mushy condition, green spots or oil spots, pitting, scale, sprouting, sprayburn, sunburn, unsightly discoloration, buckskin, melanose, scars, scab, dirt or other foreign materials, disease, insects, or mechanical or other means.

(a) Each fruit in this grade shall be reasonably well colored.

(b) In this grade not more than two-thirds of the fruit surface, in the aggregate, may be affected with light brown discoloration, or may have the equivalent of this amount in appearance when the fruit has lighter or darker shades of discoloration. (See § 51.1819.)

§ 51.1815 *U S. No. 2 Russet.* The requirements for this grade are the same as for U. S. No. 2 except that more than 20 percent, by count, of the fruits shall have in excess of two-thirds of their surface, in the aggregate, affected with light brown discoloration. (See § 51.1819.)

§ 51.1816 *U S. No. 3.* "U. S. No. 3" consists of tangerines which are mature, not flabby and not seriously lumpy, and which are free from unhealed bird pecks, unhealed skin-breaks, and decay, and free from very serious damage caused by bruises, ammoniation, creasing, dryness or mushy condition, pitting, scale, sprouting, sprayburn, sunburn, unsightly discoloration, melanose, scars,

scab, dirt or other foreign materials, disease, insects, or mechanical or other means. (See § 51.1820.)

UNCLASSIFIED

§ 51.1817 *Unclassified.* "Unclassified" consists of tangerines which have not been classified in accordance with any of the foregoing grades. The term "unclassified" is not a grade within the meaning of these standards but is provided as a designation to show that no grade has been applied to the lot.

TOLERANCES

§ 51.1818 *Tolerances.* In order to allow for variations incident to proper grading and handling in each of the foregoing grades, the tolerances set forth in §§ 51.1819 and 51.1820 are provided as specified.

§ 51.1819 *U. S. Fancy, U. S. No. 1, U. S. No. 1 Bronze, U. S No. 1 Russet, U. S. No. 2 and U. S. No 2 Russet Grades.* Not more than a total of 10 percent, by count, of the fruits in any lot may fail to meet the requirements of the grade other than for discoloration, but not more than one-half of this amount, or 5 percent, shall be allowed for very serious damage other than that caused by dryness or mushy condition, and not more than one-twentieth of the tolerance, or one-half of 1 percent, shall be allowed for decay at shipping point: *Provided,* That an additional tolerance of 2½ percent, or a total of not more than 3 percent, shall be allowed for decay en route or at destination. In addition, not more than a total of 10 percent, by count, of the fruits in any lot may not meet the requirements relating to discoloration but not more than 2 percent shall be allowed for serious damage by unsightly discoloration.

§ 51.1820 *U. S. No. 3 Grade.* Not more than a total of 15 percent, by count, of the fruits in any lot may fail to meet the requirements of this grade, but not more than one-third of this amount, or 5 percent, shall be allowed for defects other than that caused by dryness or mushy condition, and not more than one-fifteenth of the tolerance, or 1 percent, shall be allowed for decay at shipping point: *Provided,* That an additional tolerance of 2 percent, or a total of not more than 3 percent, shall be allowed for decay en route or at destination.

APPLICATION OF TOLERANCES

§ 51.1821 *Application of tolerances.* (a) The contents of individual packages in the lot, based on sample inspection, are subject to the following limitations: *Provided,* That the averages for the entire lot are within the tolerances specified for the grade.

(1) For packages which contain more than 10 pounds and a tolerance of 10 percent or more is provided, individual packages in any lot shall have not more than one and one-half times the tolerance specified. For packages which contain more than 10 pounds and a tolerance of less than 10 percent is provided, individual packages in any lot shall have not more than double the tolerance specified, except that at least one decayed or very seriously damaged fruit may be permitted in any package.

(2) For packages which contain 10 pounds or less, individual packages in any lot are not restricted as to the percentage of defects, except that not more than one fruit which is decayed or very seriously damaged shall be allowed in any package.

STANDARD PACK

§ 51.1822 *Standard pack.* (a) The tangerines in each container shall be packed in accordance with recognized methods. Each container shall be well filled and properly marked to indicate the size of the fruit. When the figures used to indicate size of fruit vary from the actual number of tangerines in the container, as in the case of fractional parts of boxes, the figures indicating size shall be followed by the letter "s" or the word "size", as, for example, "210's" or "210 size" Containers which are not so marked shall not be regarded as meeting requirements of "standard pack."

(1) Fruit in each container shall be of a size not less than the minimum diameters specified in Table I for the various packs. Packs other than those listed shall have a minimum diameter not less than that specified for the nearest count.

TABLE I

Pack:	*Diameter in inches (minimum)*
100	2 7/16
120	2 11/16
150	2 5/16
176	2 1/16
210	2 1/16
246	2 1/16
294	2

(2) In order to allow for variations incident to proper sizing, not more than 10 percent, by count, of the fruits in any lot may be below the minimum size for the count as specified in Table I.

DEFINITIONS

§ 51.1823 *Mature.* "Mature" means the same as that term is then currently prescribed for tangerines in sections 601.21 and 601.22, Chapter 20492, Florida Statutes, known as the Florida Citrus Code of 1949, or as it may be amended hereafter.

§ 51.1824 *Firm.* "Firm" means that the flesh is not soft and the fruit is not badly puffy and that the skin has not become materially separated from the flesh of the tangerine.

§ 51.1825 *Well formed.* "Well formed" means that the fruit has the characteristic tangerine shape and is not deformed.

§ 51.1826 *Damage.* "Damage" means any defect which more than slightly affects the appearance, or the edible or shipping quality of the fruit. Any one of the following defects, or any combination of defects, the seriousness of which exceeds the maximum allowed for any one defect, shall be considered as damage:

(a) Ammoniation, when it is not speck-type similar to melanose, provided that no ammoniation shall be permitted that detracts from the appearance of the individual fruit to a greater extent than the amount of discoloration allowed for the grade;

(b) Creasing, when it materially affects the appearance or shipping quality of the fruit;

(c) Dryness or mushy condition, when mushy or distinctly dry to a depth of more than one-eighth inch in all segments at the stem end, or the equivalent of this amount, by volume, of mushy condition or dryness when occurring in any portion of the fruit;

(d) Green spots or oil spots, when the appearance is affected to a greater extent than 10 green spots caused by scale, each of which is equivalent to the area of a circle one-eighth inch in diameter;

(e) Pitting, when materially affecting the appearance or shipping quality of the individual fruit;

(f) Scale, when occurring as a blotch and the aggregate area exceeds the area of a circle three-eighths inch in diameter, or any scale that detracts from the appearance of the individual fruit to a greater extent than the area permitted for a blotch. "Blotch" refers to actual scale and not the discolored area caused by scale;

(g) Sprayburn, when causing the skin to become hard or when it materially affects the appearance of the fruit;

(h) Sunburn, when causing the skin to become hard or when it materially affects the appearance of the fruit;

(i) Unsightly discoloration, when the color or the pattern, or a combination of color and pattern, causes the fruit to have an unattractive appearance;

(j) Buckskin, when it detracts from the appearance of the fruit to a greater extent than the amount of discoloration allowed for the grade;

(k) Melanose, when not small smooth speck-type, or any speck-type that detracts from the appearance of the fruit to a greater extent than the amount of discoloration allowed in the grade. Melanose that exceeds the amount allowed in the U. S. No. 1 grade is not permitted in the U. S. No. 1 Bronze grade;

(l) Scars, when not smooth, or when causing any noticeable depression, or when detracting from the appearance of the fruit to a greater extent than the amount of discoloration allowed for the grade; and,

(m) Scab, when not smooth, or when it affects shape, or when it detracts from the appearance of the fruit to a greater extent than the amount of discoloration allowed for the grade. Scab injury that exceeds the amount allowed in the U. S. No. 1 grade is not permitted in the U. S. No. 1 Bronze grade.

§ 51.1827 *Highly colored.* "Highly colored" means that the ground color of each fruit is a deep tangerine color with practically no trace of yellow color.

§ 51.1828 *Discoloration.* "Discoloration" includes discoloration caused by rust mite, melanose, scars, scab, or any other means. Shades of discoloration which blend with the ground color of the fruit may be allowed on a larger area than that specified in the grade for light brown discoloration, and shades of discoloration which are more in contrast with the ground color shall be restricted to a lesser area: *Provided,* That no discoloration may affect the appearance to a greater extent than the amount of

light brown discoloration specified for the grade. Tangerines which show discoloration caused by melanose, scab, or any cause other than by thrip, wind scars, or by rust mite shall not be permitted in the U. S. No. 1 Bronze grade when such discoloration exceeds the amount allowed in the U. S. No. 1 grade. (See § 51.1830.)

§ 51.1829 *Fairly well colored.* "Fairly well colored" means that the surface of the fruit may have green color which does not exceed the aggregate area of a circle one inch in diameter and that the remainder of the surface, which is not discolored, shows at least a good yellow color: *Provided,* That some portion of the surface shows a reddish tangerine blush.

§ 51.1830 *Bronzed russeting.* "Bronzed russeting" means russeting caused by thrip, wind scars, or by rust mite, or similar russeting which is not readily distinguishable from that caused by rust mite. Discoloration caused by melanose, scab, etc., are not considered as "bronzed russeting" within the meaning of these standards but are regarded as defects when they exceed the amounts permitted in the U. S. No. 1 grade and are not permitted in the U. S. No. 1 Bronze grade.

§ 51.1831 *Fairly firm.* "Fairly firm" means that the flesh may be slightly soft but is not bruised or badly puffy, and that the skin has not become seriously separated from the flesh of the tangerine.

§ 51.1832 *Fairly well formed.* "Fairly well formed" means that the fruit may not have the shape characteristic of the variety but that it is not badly deformed.

§ 51.1833 *Serious damage.* "Serious damage" means any defect which seriously affects the appearance, or the edible or shipping quality of the fruit. Any one of the following defects, or any combination of defects, the seriousness of which exceeds the maximum allowed for any one defect, shall be considered as serious damage:

(a) Ammoniation, when scars are cracked, or when dark and the aggregate area exceeds the area of a circle one-half inch in diameter, or when light colored and the aggregate area exceeds the area of a circle 1 inch in diameter;

(b) Creasing, when it causes the skin to be seriously weakened;

(c) Dryness or mushy condition, when mushy or distinctly dry to a depth of more than one-fourth inch in all segments at the stem end, or the equivalent of this amount, by volume, of mushy condition or dryness when occurring in any portion of the fruit;

(d) Green spots or oil spots, when the appearance is affected to a greater extent than 25 green spots, caused by scale, each of which is equivalent to the area of a circle one-eighth inch in diameter;

(e) Pitting, when seriously affecting the appearance or shipping quality of the fruit;

(f) Scale, when occurring as a blotch and the aggregate area exceeds the area of a circle one-half inch in diameter, or any scale that detracts from the appearance of the fruit to a greater extent than the area permitted for a blotch. "Blotch" refers to actual scale and not the discoloration caused by scale;

(g) Sprayburn, when it has caused the skin to become hard, or when it seriously affects the appearance of the fruit;

(h) Sunburn, when it has caused the skin to become hard, or when it seriously affects the appearance of the fruit;

(i) Unsightly discoloration, when the color or the pattern, or a combination of both, causes the fruit to have a distinctly unattractive appearance;

(j) Buckskin, when it detracts from the appearance of the fruit to a greater extent than the amount of discoloration allowed for the grade;

(k) Melanose, when badly caked and the aggregate area exceeds the area of a circle one-half inch in diameter, or when lightly caked and the aggregate area exceeds the area of a circle 1 inch in diameter, or when unsightly or when it detracts from the appearance of the fruit to a greater extent than the amount of discoloration allowed for the grade;

(l) Scars, when not fairly smooth, or when causing any materially depressed areas, or when detracting from the appearance to a greater extent than the amount of discoloration allowed for the grade. Scars which are not fairly smooth, or which are materially depressed, are not permitted in either U. S. No. 2 or U. S. No. 2 Russet grades; and,

(m) Scab, when not fairly smooth or when it materially affects the shape of the fruit, or when it detracts from the appearance to a greater extent than the maximum amount of discoloration allowed for the grade.

§ 51.1834 *Reasonably well colored.* "Reasonably well colored" means that a good yellow or reddish tangerine color shall predominate over the green color on at least one-half of the fruit surface in the aggregate, and that each fruit shall show practically no lemon color.

§ 51.1835 *Very serious damage.* "Very serious damage" means any defect which seriously affects the appearance, or the edible or shipping quality of the fruit. Any one of the following defects, or any combination of defects, the seriousness of which exceeds the maximum allowed for any one defect, shall be considered as very serious damage:

(a) Ammoniation, when scars are badly cracked, or when dark and the aggregate area exceeds the area of a circle 1 inch in diameter, or when light colored and it detracts from the appearance of the fruit to a greater extent than the area permitted for dark ammoniation;

(b) Creasing, when causing the skin to be seriously weakened;

(c) Dryness or mushy condition, when mushy or distinctly dry to a depth of more than one-fourth inch in all segments at the stem end, or the equivalent of this amount, by volume, of mushy condition or dryness when occurring in any portion of the fruit;

(d) Pitting, when it very seriously affects the appearance or the shipping quality of the fruit;

(e) Scale, when it very seriously affects the appearance of the fruit;

(f) Sprayburn, when it very seriously affects the appearance of the fruit;

(g) Sunburn, when it very seriously affects the appearance of the fruit;

(h) Unsightly discoloration, when the fruit has a very objectionable appearance caused by any means. The color or the pattern of the discoloration, or a combination of both, or a combination of defects may cause the fruit to have a very unsightly appearance;

(i) Melanose, when caked to the extent that the appearance of the fruit is very seriously affected;

(j) Scars, when so deep, rough, or unsightly that the appearance of the fruit is very seriously injured; and,

(k) Scab, when it causes the fruit to be very seriously injured.

§ 51.1836 *Diameter* "Diameter" means the greatest dimension measured at right angles to a line from stem to blossom end of the fruit.

The United States Standards for Florida Tangerines contained in this subpart shall become effective 30 days after publication hereof in the FEDERAL REGISTER, and will thereupon supersede the United States Standards for Florida Tangerines which have been in effect since October 18, 1952 (§§ 51.1810 to 51.1836)

Dated. August 9, 1955.

[SEAL] ROY W. LENNARTSON,
Deputy Administrator,
Marketing Services.

[F. R. Doc. 55-6584; Filed, Aug. 11, 1955; 8:50 a. m.]

Chapter IX—Agricultural Marketing Service (Marketing Agreements and Orders), Department of Agriculture

[958.319 Amdt. 1]

PART 958—IRISH POTATOES GROWN IN COLORADO

LIMITATION OF SHIPMENTS

Findings. (a) Pursuant to Marketing Agreement No. 97 and Order No. 58 (7 CFR Part 958; 19 F. R. 9368), regulating the handling of Irish potatoes grown in the State of Colorado, effective under the applicable provisions of the Agricultural Marketing Agreement Act of 1937, as amended (48 Stat. 31, as amended; 7 U. S. C. 601 et seq.) and upon the basis of the recommendation and information submitted by the area committee for Area No. 3, established pursuant to said marketing agreement and order, and upon other available information, it is hereby found that the amendment to the limitation of shipments, as herein provided, will tend to effectuate the declared policy of the act.

(b) It is hereby found that it is impracticable and contrary to the public interest to give preliminary notice, engage in public rule making procedure, and postpone the effective date of this amendment until 30 days after publication in the FEDERAL REGISTER (5 U. S. C. 1001 et seq.) in that (i) the time intervening between the date when informa-

tion upon which this amendment is based became available and the time when this amendment must become effective in order to effectuate the declared policy of the act is insufficient, (ii) more orderly marketing in the public interest, than would otherwise prevail, will be promoted by regulating the shipment of potatoes, in the manner set forth below, on and after the effective date of this amendment, (iii) compliance with this amendment will not require any special preparation on the part of handlers which cannot be completed by the effective date, (iv) reasonable time is permitted, under the circumstances, for such preparation, and (v) information regarding the committee's recommendations has been made available to producers and handlers in the production area.

Order as amended. The provisions of § 958.319 (b) (1) (FEDERAL REGISTER, July 20, 1955, 20 F. R. 5155) are hereby amended to read as follows:

(b) *Order* (1) During the period from August 15, 1955 to May 31, 1956, both dates inclusive, no handler shall ship any potatoes (i) of the Early Gem variety unless such potatoes are of a size not smaller than 2¼ inches minimum diameter or five ounces minimum weight, and meet the requirements of the U. S. No. 2, or better grade, (ii) of the other long varieties (including, but not limited to, White Rose and Russet Burbank) unless such potatoes are of a size not less than five ounces minimum weight, and meet the requirements of the U. S. No. 2, or better grade; and (iii) of the round varieties (including, but not limited to, Irish Cobbler, Katahdin, Kennebec, Bliss Triumph and Pontiac) unless such potatoes are of a size not smaller than 2¼ inches minimum diameter, and meet the requirements of the U. S. No. 2, or better grade, except that such potatoes must be fairly well shaped, free from damage caused by second growth, growth cracks, sunburn, and cuts, free from surface scab which covers an area of more than 25 percent of the surface of the potato in the aggregate, and free from pitted scab which affects the appearance of the potato to a greater extent than the amount of the surface scab permitted: *Provided,* That an additional tolerance of five percent shall be allowed for potatoes which do not meet the above specified marketing limitations for shape and scab, and damage from second growth, growth cracks, sunburn, and cuts, but such potatoes must meet the requirements of the U. S. No. 2 grade, as such terms, grades, and sizes are set forth in the United States Standards for Potatoes (§§ 51.1540 to 51.1559 of this title) including the tolerances set forth therein.

(Sec. 5, 49 Stat. 753, as amended; 7 U. S. C. 608c)

Done at Washington, D. C., this 10th day of August 1955, to become effective August 15, 1955.

[SEAL] S. R. SMITH,
Director
Fruit and Vegetable Division.

[F. R. Doc. 55-6602; Filed, Aug 11, 1955; 8:51 a. m.]

PART 993—DRIED PRUNES PRODUCED IN CALIFORNIA

ORDER FINDING THAT ESTIMATED SEASONAL AVERAGE PRICE OF PRUNES FOR CROP YEAR WHICH BEGAN AUGUST 1, 1955, WILL BE IN EXCESS OF PARITY AND PROVIDING FOR SPECIAL REGULATION OF PRUNES

This action is being taken pursuant to the provisions of § 993.50 of Marketing Agreement No. 110, as further amended, and Marketing Order No. 93, as further amended (19 F. R. 1301) regulating the handling of dried prunes produced in California, effective under the Agricultural Marketing Agreement Act of 1937, as amended (7 U. S. C. 601 et seq.) In paragraph (a) of said § 993.50 it is provided that, if the Secretary of Agriculture should find that the estimated seasonal average price for prunes for any crop year will be in excess of the price level contemplated by the provisions of section 2 (1) of the act, he shall issue an order in which such finding is set forth, and, in such order, he may provide that, for such crop year, the handling of prunes shall be in accordance with the provisions set forth in paragraphs (b), (c) (d) (e) and (f) of that section.

On the basis of information which has been received from the Prune Administrative Committee (the administrative agency for the operation of this program) and other pertinent information which is available to this Department, it appears that: (a) The total supply of California dried prunes (natural condition weight) during the 1955–56 crop year, including the estimated handler carry-in as of August 1, 1955, will approximate 175,000 tons, as compared with a supply of about 194,000 tons a year earlier; (b) during the 1954–55 crop year, returns to producers averaged $212 per ton, or approximately 98 percent of the July 15, 1955, parity price for prunes; (c) the 1955 prune production will contain a higher percentage of the larger sizes of prunes and a lower percentage of the smaller sizes of prunes than were contained in the 1954 production, and this situation should tend to increase the average returns to the producers; (d) domestic consumption of dried prunes is likely to remain at high levels during the 1955–56 crop year, due to such factors as population increases in the United States, favorable levels of consumer income, and the trade promotion activities of the dried prune industry; and (e) moderate increases in exports of dried prunes probably will result from liberalization of import trade barriers by some foreign countries and the allocation of United States dollars by or to importing countries for purchases of dried fruit.

On the basis of the aforementioned existing and prospective situation with respect to prunes, it is hereby found and determined that the estimated seasonal average price for prunes for the crop year which began on August 1, 1955 will be in excess of the price level contemplated by the provisions of section 2 (1) of the aforementioned act (i. e., such estimated seasonal average price for prunes will exceed parity for that crop year) It is further found and determined that the provisions of paragraphs (b), (c) (d) (e) and (f) of said § 993.50 will tend to effectuate, on and after the effective date of this order, the declared policy of the act during the crop year which began on August 1, 1955:

It is therefore ordered, That such provisions shall apply to all handlings of prunes during said crop year after the effective date of this order:

It is further ordered, That any and all surplus tonnage prunes held by handlers and referable to their acquisitions of prunes during said crop year which began on August 1, 1955 shall, as soon as practicable after the effective time of this order, be released to the respective handlers for disposition as parts of their salable tonnages.

This regulation of prunes for the remainder of the 1955–56 crop year is considered to be necessary to assure the marketing of only those prunes which are of a quality reasonably satisfactory to consumers, to promote the interests of the dried prune industry, and to establish such orderly marketing of prunes as will be in the public interest.

It is also hereby found and determined that notice of proposed rule making, public participation therein, and 30 day's notice prior to its effective date (see section 4 of the Administrative Procedure Act; 5 U. S. C. 1001 et seq.) is impracticable, unnecessary, and contrary to the public interest. The effect of this action will be to reduce the restrictions which would otherwise be applicable. The crop year in question has already begun, and it is imperative that this action be made effective as soon as possible. The possibility that this action would be taken is already well known to the prune industry. It will require no advance preparation by prune handlers. In order to effectuate the declared policy of the act, this order must become effective on the date of its publication in the FEDERAL REGISTER.

(Sec. 5, 49 Stat. 753, as amended; 7 U. S. C. 608c)

Issued at Washington, D. C. this 8th day of August 1955, to become effective on the date on which this order is published in the FEDERAL REGISTER.

[SEAL] S. R. SMITH,
Director
Fruit and Vegetable Division.

[F. R. Doc. 55-6571; Filed, Aug. 11, 1955; 8:48 a. m.]

TITLE 14—CIVIL AVIATION

Chapter II—Civil Aeronautics Administration, Department of Commerce

[Amdt. 126]

PART 608—RESTRICTED AREAS

ALTERATIONS

The restricted area alterations appearing hereinafter have been coordinated with the civil operators involved, the Army, the Navy and the Air Force,

through the Air Coordinating Committee, Airspace Panel, and are adopted to become effective when indicated in order to promote safety of the flying public. Since a military function of the United States is involved, compliance with the notice, procedure, and effective date provisions of section 4 of the Administrative Procedure Act is not required.

Part 608 is amended as follows:

1. In § 608.14, the El Centro, California, area (R–302 formerly D–302), amended on May 10, 1951, in 16 F R. 4311, is redesignated as follows:

Name and location (chart)	Description by geographical coordinates	Designated altitudes	Time of designation	Controlling agency
EL CENTRO (R–302) (San Diego).	Beginning at latitute 32°59'35" longitude 115°43'30"; thence to latitude 32°52'40" longitude 115°43'30"; thence southwesterly around the perimeter of NAAS El Centro Control Zone to latitude 32° 50'05", longitude 115°44'30"; thence to latitude 32°50'05" longitude 115°55'00"; thence to latitude 32°55'50" longitude 115°55'00"; thence to latitude 33°01'20" longitude 116°02'15"; thence to latitude 33°06'35" longitude 115°56'50"; thence to latitude 33°06'35" longitude 115°51'12"; thence to point of beginning.	Surface to unlimited.	Continuous.	Fleet Air Detachment, El Centro, Calif.

2. In § 608.14, the Salton Sea, California, area (R–303 formerly D–303) amended on June 3, 1952, in 17 F R. 4977, is redesignated as follows:

Name and location (chart)	Description by geographical coordinates	Designated altitudes	Time of designation	Controlling agency
SALTON SEA (R–303) (San Diego).	Beginning at latitude 33°18'00" longitude 115°44'00"; thence to latitude 33°10'40", longitude 115°44'00"; thence to latitude 33°10'40", longitude 115°49'50"; thence to latitude 33° 23'15", longitude 115°58'40"; thence to latitude 33°26'15" longitude 115°54'00"; thence to point of beginning.	Surface to unlimited.	Continuous.	CO NAAS El Centro Calif.

(Sec. 205, 52 Stat. 984, as amended; 49 U. S. C. 425. Interpret or apply sec. 601, 52 Stat. 1007, as amended; 49 U. S. C. 551)

This amendment shall become effective on August 25, 1955.

[SEAL] F B. LEE,
Administrator of Civil Aeronautics.

[F R. Doc. 55–6558; Filed, Aug. 11, 1955; 8:45 a. m.]

[Amdt. 127]

PART 608—RESTRICTED AREAS

ALTERATIONS

The restricted area alterations appearing hereinafter have been coordinated with the civil operators involved, the Army, the Navy and the Air Force, through the Air Coordinating Committee, Airspace Panel, and are adopted to become effective when indicated in order to promote safety of the flying public. Since a military function of the United States is involved, compliance with the notice, procedure, and effective date provisions of section 4 of the Administrative Procedure Act is not required.

Part 608 is amended as follows:

1. In § 608.14, the Chocolate Mountains, California, area (R–304 formerly D–304) amended on November 10, 1953, in 18 F R. 7056, is redesignated as follows:

Name and location (chart)	Description by geographical coordinates	Designated altitudes	Time of designation	Controlling agency
CHOCOLATE MOUNTAINS, (R–304) (San Diego).	Beginning at latitude 33°32'40" N., longitude 115°33'50" W., SE along a road at latitude 33°25'50" N., longitude 115°14'30" W. southwest to latitude 33°21'15" N., longitude 115° 17'00" W., southeast and northeast along a road to latitude 33°22'50" N., longitude 115° 09'58" W.; southeast to latitude 33°08'45" N., longitude 114°56'40" W., southwest to latitude 33°01'00" N., longitude 115°06'00" W., northwest to latitude 33°23'30" N., longitude 115°42'10" W.; northeast to latitude 33°32'40" N., longitude 115°33'50" W., point of beginning. Except for that portion which is in conflict with Victor civil airway 117.	Surface to unlimited.	24 hours daily.	Fleet Air Detachment, El Centro, Calif.

2. In § 608.41, the Cherry Point, North Carolina, area #2 (R–125 formerly D–125) amended on June 9, 1955, in 20 F R. 4002, is further amended by changing the "Description by Geographical Coordinates" column to read: "Beginning at latitude 35°46'30" longitude 76°47'00" southwesterly along the east edge of Amber civil airway No. 9 to latitude 34°21'40" longitude 77°41'30" clockwise along the arc of a circle with a radius of 60 statute miles centered at latitude 34°54'30" longitude 76°53'00" to latitude 34°27'10" longitude 77°47'45" north along the eastern boundary of airway V–157 to latitude 35°29'00" longitude 77°40'20" clockwise along the arc of a circle with a radius of 60 statute miles centered at latitude 34°54'30" longitude 76°53'00" to latitude 35°46'30" longitude 76°47'00" point of beginning. And by adding to the "Designated Altitude" column: "West of Amber civil airway No. 9 from 6000 feet MSL to unlimited, from sunset to sunrise."

(Sec. 205, 52 Stat. 984, as amended; 49 U. S. C. 425. Interpret or apply sec. 601, 52 Stat. 1007, as amended; 49 U. S. C. 551)

This amendment shall become effective on August 25, 1955.

[SEAL] F B. LEE,
Administrator of Civil Aeronautics.

[F. R. Doc. 55–6559; Filed, Aug. 11, 1955; 8:45 a. m.]

TITLE 19—CUSTOMS DUTIES

Chapter I—Bureau of Customs, Department of the Treasury

[T. D. 53868]

PART 30—FOREIGN-TRADE ZONES

DESIGNATION OF CONSIGNEE AND OWNER FOR CUSTOMS PURPOSES OF PRIVILEGED FOREIGN MERCHANDISE

Whereas the Customs Regulations do not specify for privileged foreign merchandise who shall be accepted by the collector of customs as the consignee and owner thereof for customs purposes, §§ 30.6 and 30.14 of the Customs Regulations are hereby amended to provide therefor as follows:

1. Section 30.6 is amended by adding new paragraph (j), as follows:

(j) The original of the application on zone Form B when approved by the zone grantee shall be accepted by the collector as the equivalent of a bill of lading or carrier's certificate to identify the person designated in such Form B as the consignee of the merchandise and its owner for customs purposes, except that such person may transfer the right to withdraw such merchandise from the zone to customs territory in accordance with § 30.14 (f)

2a. Section 30.14 is amended by redesignating paragraphs (f) through (n) as (g) through (o) and adding new paragraph (f), as follows:

(f) The applicant on customs Form 7505 or 7519 for purposes described in paragraph (b) (c) or (d) of this section shall be the consignee named in zone Form B as approved by the grantee (see § 30.6 (j)) except that such consignee may transfer the right to transfer the merchandise from the zone to customs territory by an endorsement on customs Form 7505 or 7519, whichever is applicable, naming a designated transferee. Customs Form 7505 or 7519 so endorsed with the name of a designated transferee who has been approved by the grantee shall be accepted by the collector to identify the transferee named therein as the consignee of the merchandise to be transferred and the owner thereof for customs purposes.

b. In redesignated paragraphs (j) and (l) the reference to paragraph "(g)" is changed to "(h)"; in redesignated paragraph (m) the reference to paragraph "(k)" is changed to "(l)"; in redesignated paragraph (n) the references to paragraphs "(f) to (j)" and paragraph "(h)" are changed to "(g) to (k)" and "(i)", respectively.

3. In § 30.17 (a) the reference to "§ 30.14 (f) through (i)" is changed to "§ 30.14 (g) through (j)".

(R. S. 161, 251, secs. 1–21, 48 Stat. 998, 999, as amended, 1000–1003, sec. 624, 46 Stat. 759; 5 U. S. C. 22, 19 U. S. C. 66, 81a–81u, 1624)

[SEAL] RALPH KELLY,
Commissioner of Customs.

Approved: August 3, 1955.

H. CHAPMAN ROSE,
Acting Secretary of the Treasury.

[F. R. Doc. 55–6573; Filed, Aug. 11, 1955; 8:48 a. m.]

TITLE 29—LABOR

Chapter V—Wage and Hour Division, Department of Labor

PART 711—ELECTRICAL, INSTRUMENT, AND RELATED MANUFACTURING INDUSTRIES IN PUERTO RICO

MINIMUM WAGE ORDER

Pursuant to the provisions of the Administrative Procedure Act (5 U. S. C. 1001) notice was published in the FEDERAL REGISTER on August 2, 1955 (20 F. R. 5503) of my proposed decision to approve the recommendations of Special Industry Committee No. 16–A for the Electrical, Instrument, and Related Manufacturing Industries in Puerto Rico, together with the wage order which I proposed to issue to carry such decision into effect.

As indicated in the notice, my findings and conclusions in this matter were set forth in a document entitled "Findings and Opinion in the Matter of the Recommendations of Special Industry Committee No. 16–A for Puerto Rico for Minimum Wage Rates in the Electrical, Instrument, and Related Manufacturing Industries in Puerto Rico."

Since a bill entitled "Fair Labor Standards Amendments of 1955" which was recently approved by the Congress, will require a different procedure for the promulgation of wage orders for Puerto Rico, if and when approved by the President, it is essential to expedite all such matters now pending in the Department of Labor in order to prevent the loss of time, effort, and money already invested in them. In view of these circumstances, consideration was given to the fact that section 8 (c) of the Administrative Procedure Act (5 U. S. C. 1001) permits the Agency to omit tentative decisions "in any case in which the agency finds upon the record that due and timely execution of its functions imperatively so requires" It was therefore found upon the record that due and timely execution of the functions of this agency in these circumstances did not require the total elimination of the tentative decision to approve the recommendations of Special Industry Committee No. 16–A for the Electrical, Instrument, and Related Manufacturing Industries in Puerto Rico, but did require shortening the usual period for filing exceptions to five days. This period has now expired.

The only exceptions that have been filed are those on behalf of The Electronic Industries Association of Puerto Rico and Sprague Caribe Company to the effect that the minimum hourly wage of 70 cents for the General Division of the Industry would cause substantial curtailment of employment. The arguments now submitted in support of these exceptions were urged by counsel for this Association and this Company at the hearing on the Committee's recommendations. These arguments have been considered and are discussed in the Findings and Opinion referred to in my Notice of Proposed Decision. It appears, therefore, that no further discussion of them is appropriate, and they are overruled.

Accordingly, pursuant to authority under the Fair Labor Standards Act of 1938 (29 U. S. C. 201 et seq.) Reorganization Plan No. 6 of 1950 (5 U. S. C. 611), General Order No. 45–A (15 F. R. 3290) and, the position of the Administrator being presently vacant, General Order No. 85 (20 F. R. 2066), the said decision is affirmed and made final; the recommendations of Special Industry Committee No. 16–A for minimum wage rates in the Electrical, Instrument, and Related Manufacturing Industries in Puerto Rico are hereby approved; and a wage order, designated as Part 711 (29 CFR, Part 711), is hereby issued to read as follows:

Sec.
711.1 Approval of recommendations of industry committee.
711.2 Wage rates.
711.3 Notice of order.
711.4 Definition of the electrical, instrument, and related manufacturing industries in Puerto Rico, and divisions thereof.

AUTHORITY: §§ 711.1 to 711.4 issued under sec. 8, 52 Stat. 1064, as amended, 29 U. S. C. 208.

§ 711.1 *Approval of recommendations of industry committee.* The committee's recommendations are hereby approved.

§ 711.2 *Wage rates.* (a) Wages at a rate of not less than 60 cents an hour shall be paid under section 6 of the Fair Labor Standards Act of 1938, as amended, by every employer to each of his employees in the lens and thermometer division of the electrical, instrument, and related manufacturing industries in Puerto Rico who is engaged in commerce or in the production of goods for commerce.

(b) Wages at a rate of not less than 65 cents an hour shall be paid under section 6 of the Fair Labor Standards Act of 1938, as amended, by every employer to each of his employees in the resistance-type household appliance division of the electrical, instrument, and related manufacturing industries in Puerto Rico who is engaged in commerce or in the production of goods for commerce.

(c) Wages at a rate of not less than 70 cents an hour shall be paid by every employer to each of his employees in the general division of the electrical, instrument, and related manufacturing industries in Puerto Rico who is engaged in commerce or in the production of goods for commerce.

§ 711.3 *Notice of order* Every employer employing any employees so engaged in commerce or in the production of goods for commerce in the electrical, instrument, and related manufacturing industries in Puerto Rico shall post in a conspicuous place in each department of his establishment where such employees are working such notices of this order as shall be prescribed, from time to time, by the Wage and Hour Division of the United States Department of Labor and shall give such other notice as the Division may require.

§ 711.4 *Definition of the electrical, instrument, and related manufacturing industries in Puerto Rico, and divisions thereof.* (a) (1) The electrical, instrument, and related manufacturing industries in Puerto Rico to which this part shall apply are hereby defined as follows: The manufacture, assembly, or repair of machinery, apparatus or equipment and supplies for the generation, storage, transmission, transportation, or utilization of electrical energy, and the manufacture, assembly, or repair of instruments, apparatus, and equipment for scientific, professional, industrial, industrial-measurement, photographic, musical or horological purposes: *Provided, however,* That the definition shall not include (i) industrial and commercial machinery powered by electric motors, (ii) measuring-and-dispensing pumps, or (iii) any activity included in the clay and clay products industry, the jewel cutting and polishing industry, or the stone, glass, and related products industry as defined in the wage orders for those industries in Puerto Rico.

(2) The definition contained in subparagraph (1) of this paragraph supersedes the definition contained in any and all wage orders issued heretofore for other industries in Puerto Rico to the extent that such definitions include products or operations covered by the definition of these industries.

(b) The separable divisions of the industries defined in paragraph (a) (1) of this section to which this part shall apply are hereby defined as follows:

(1) *Lens and thermometer division.* This division consists of the grinding and manufacture of optical and ophthalmic lenses and prisms and the manufacture of glass thermometers and hydrometers.

(2) *Resistance-type household appliance division.* This division consists of the manufacture of household electrical appliances of the resistance type and parts therefor, used for heating, cooking and other purposes (except illumination), including, but without limitation, electric ranges, stoves, hotplates, cookers, casseroles, roasters, toasters, heaters, irons, and percolators.

(3) *General division.* This division consists of all products and activities included in the electrical, instrument, and related manufacturing industries, as defined in paragraph (a) (1) of this section, except products and activities included in the lens and thermometer division and the resistance-type household appliance division as defined in this part.

This wage order shall become effective September 12, 1955.

Signed at Washington, D. C., this 9th day of August 1955.

STUART ROTHMAN,
Solicitor of Labor.

[F. R. Doc. 55–6585; Filed, Aug. 11, 1955; 8:50 a. m.]

TITLE 38—PENSIONS, BONUSES, AND VETERANS' RELIEF

Chapter I—Veterans Administration

PART 3—VETERANS CLAIMS

PROCUREMENT OF AUTOMOBILES AND OTHER CONVEYANCES FOR DISABLED VETERANS

In § 3.1500, paragraph (d) is amended to read as follows:

§ 3.1500 *Procurement of automobiles and other conveyances for disabled veterans.* * * *

(d) *Time limit for filing claim.* Under the provisions of section 5 as amended by Public Law 92, 84th Congress, veterans within the purview of the legislation may file an application for such benefits:

(1) Within 5 years after October 20, 1951, or within 5 years after the date of the veteran's discharge or release from active World War II or Korean Conflict service if the veteran is not discharged or released until after October 20, 1951.

(2) Within 3 years after occurrence of the disability in the case of any veteran whose qualifying conditions occurred subsequent to his discharge or release from active World War II or Korean Conflict service. (The purpose of this provision of the law may be illustrated by the case of a veteran who is discharged with an injury to one of his feet. Treatment is given over a number of years, but eventually amputation is directed by the physician. The time for filing may have expired or so nearly so as not to permit the veteran to meet such time limit in view of the existing circumstances. This provision of the law would grant such a veteran three years from the date of the occurrence of the required disability to file for his grant towards the purchase of a car.)

(3) Within one year from the date on which entitlement to compensation for the required conditions shall have been determined. (The purpose of this provision is to grant a period of one year from the date service connection is initially established for one of the entitling conditions in claims in which service connection was not established until after the basic time for filing had expired. This may be illustrated by a veteran whose case was not adjudicated or allowed by the Board of Veterans Appeals until after the basic time for filing for a car had expired.) (Instruction 1–A, Public Law 187, 82d Congress, as amended by Public Law 92, 84th Congress.)

(Sec. 5, 43 Stat. 608, as amended, sec. 2, 46 Stat. 1016, sec. 7, 48 Stat. 9; 38 U. S. C. 11a, 426, 707)

This regulation is effective August 12, 1955.

[SEAL] J. C. PALMER,
Assistant Deputy Administrator

[F. R. Doc. 55–6578; Filed, Aug. 11, 1955; 8:49 a. m.]

PART 36—SERVICEMEN'S READJUSTMENT ACT OF 1944

SUBPART A—TITLE III; LOAN GUARANTY

1. In § 36.4301, a new paragraph (hh) is added as follows:

§ 36.4301 *Definitions.* * * *

(hh) "Registered mail." The term "registered mail" wherever used in the regulations concerning guaranty or insurance of loans to veterans shall include certified mail.

2. In § 36.4302, paragraphs (a) (1) (2) and (3) and (c) are amended to read as follows:

§ 36.4302 *Computation of guaranties or insurance credits.* (a) For the purpose of computing guaranty in respect to a loan to a veteran, the following maxima cannot be exceeded:

(1) 501 (b) and 501 (c) Loans: 60 percent of the original principal amount, or $7,500, whichever is less.

(2) Real estate loans except 501 (b) and 501 (c) Loans: 50 percent of the original principal amount, or $4,000, whichever is less.

(3) Non-real estate loans except 501 (b) and 501 (c) Loans: 50 percent of the original principal amount, or $2,000, whichever is less.

* * * * *

(c) Subject to the provisions of paragraph (g) of § 36.4303, the following formula shall govern the ascertainment of the amount of the guaranty or insurance entitlement which remains available to an eligible veteran after prior use of entitlement: Add to the amount of such entitlement previously used for realty, twice the amount previously used for nonrealty purposes. Subtract this sum from $4,000. The sum remaining is the amount available for the guaranty or insurance of a real estate loan other than a section 501 (b) or 501 (c) loan and one-half of such sum is available for a non-real estate loan. For the purpose of ascertaining the amount of guaranty entitlement which remains available for a section 501 (b) or 501 (c) loan after prior use of entitlement, add to the amount of such entitlement previously used for realty, twice the amount previously used for nonrealty purposes. Subtract this sum from $7,500. The sum remaining is the amount of entitlement available for section 501 (b) or 501 (c) purposes.

* * * * *

3. In paragraph (a) of § 36.4306, subparagraph (4) is amended and new subparagraph (5) is added as follows:

§ 36.4306 *Refunding of outstanding indebtedness.* (a) * * *

(4) Such obligation is eligible under section 507 of the act, or

(5) If the indebtedness is secured by a lien against land owned by the veteran on which a farm residence is to be constructed with the loan proceeds, a portion of the loan proceeds may be expended to liquidate such lien, but only if the reasonable value of the land is equal to or in excess of the amount of the lien.

* * * * *

4. Section 36.4346 is revised to read as follows:

§ 36.4346 *Purchase, construction, repair, alteration, or improvement of a farm residence.* (a) No loan for the purchase, construction, alteration, improvement, or repair of a farm residence shall be eligible for guaranty or insurance pursuant to section 501 (c) of the act unless such loan is approved by the Administrator prior to disbursement, nor shall any loan for constructing or improving a farmhouse be eligible for guaranty or insurance pursuant to section 502 (b) of the act unless approved by the Administrator prior to disbursement.

(b) No loan made for any of the purposes specified in section 501 (c) of the act shall be eligible for guaranty thereunder if made in combination with a section 502 or section 503 loan.

(Sec. 504, 58 Stat. 293, as amended; 38 U. S. C. 694d)

This regulation is effective August 12, 1955.

[SEAL] J. C. PALMER,
Assistant Deputy Administrator

[F. R. Doc. 55–6577; Filed, Aug. 11, 1955; 8:49 a. m.]

TITLE 43—PUBLIC LANDS: INTERIOR

Chapter I—Bureau of Land Management, Department of the Interior

Appendix C—Public Land Orders

[Public Land Order 1176]

ARIZONA AND COLORADO

RESERVATION OF LANDS WITHIN NATIONAL FORESTS AS ADMINISTRATIVE SITES, RECREATION AREAS, OR FOR OTHER PUBLIC PURPOSES; REVOKING DEPARTMENTAL ORDER OF MAY 28, 1907

Correction

In F R. Document 55–5267, appearing in the issue for Friday, July 1, 1955, on page 4687 insert the date "June 27, 1955" at the end of the document.

[Public Land Order 1201]

WYOMING

REVOKING PUBLIC LAND ORDER 811 OF MARCH 7, 1952, WHICH WITHDREW PUBLIC LANDS AND RESERVED MINERALS IN PATENTED LANDS FOR USE OF THE UNITED STATES ATOMIC ENERGY COMMISSION

Correction

In Federal Register Document 55–6419, published at page 5686 in the issue for Saturday, August 6, 1955, the land description in paragraph 3 for section 26 of T. 43 N., R. 76 W., should read as follows: "Sec. 26, N½NE¼, SE¼NE¼, W½NW¼, SW¼, SW¼SE¼;"

[Public Land Order 1203]

ALASKA

WITHDRAWING PUBLIC LAND FOR USE OF DEPARTMENT OF THE AIR FORCE FOR MILITARY PURPOSES

By virtue of the authority vested in the President and pursuant to Executive Order No. 10355 of May 26, 1952, it is ordered as follows:

Subject to valid existing rights, the following-described public land in Alaska is hereby withdrawn from all forms of appropriation under the public-land laws, including the mining and mineral-leasing laws, and reserved for use of the Department of the Air Force for military purposes:

FAIRBANKS MERIDIAN

T. 2 S., R. 3 E. (unsurveyed),
Sec. 22, SE¼SE¼,
Sec. 23, NW¼SE¼.
T. 2 S., R. 4 E. (unsurveyed),
Sec. 17, SW¼,
Sec. 18, SE¼,
Sec. 19, N½,
Sec. 20, NW¼.
T. 2 S., R. 3 E. (surveyed),
Sec. 27, E½.

The areas described aggregate 1,200 acres.

ORME LEWIS,
Assistant Secretary of the Interior

AUGUST 8, 1955.

[F. R. Doc. 55-6561; Filed, Aug. 11, 1955; 8:46 a. m.]

[Public Land Order 1204]

CALIFORNIA

TRANSFERRING JURISDICTION OVER THE OIL AND GAS DEPOSITS IN CERTAIN LANDS OWNED BY THE UNITED STATES

Whereas the hereinafter-described lands, title to which has been acquired by the United States, comprising the U. S. Naval Ammunition and Net Depot, Seal Beach, California, are reported to be subject to drainage of their oil and gas deposits by wells on adjacent lands in private ownership; and

Whereas it is necessary in the public interest that such protective action be taken as will prevent loss to the United States by reason of the drainage or threatened drainage from the said lands; and

Whereas, in order to facilitate such action, it is considered advisable that jurisdiction over the oil and gas deposits in such lands be transferred from the Department of the Navy to the Department of the Interior; and

Whereas such transfer has the concurrence of the Secretary of the Navy:

Now, therefore, by virtue of the authority vested in the President and pursuant to Executive Order No. 10355 of May 26, 1952, it is ordered as follows:

1. The jurisdiction over the oil and gas deposits in the following-described lands is hereby transferred from the Department of the Navy to the Department of the Interior:

AREA No. 1

The east one-half of Section 5, Township 5 South, Range 11 West, more particularly described as follows:

Beginning at the point of intersection of the center lines of Garden Grove Avenue and Bolsa Chica Road, thence southerly with the center line of Bolsa Chica Road for a distance of 5294.71 feet to a point of intersection with the center line of West Seventeenth Street; thence westerly with the center line of West Seventeenth Street 2,661.18 feet to the North and South center line of Section 5, T. 5 S., R. 11 W; thence northerly with the North and South center line of said Section 5, 5,295 feet more or less, to the center line of Garden Grove Avenue; thence easterly with the center line of Garden Grove Avenue 2,659.63 feet to the center line of Bolsa Chica Road, the point of beginning.

AREA No. 2

Beginning at the point of intersection of the center lines of Bolsa Chica Road and Smeltzer Avenue, thence westerly with the center line of Smeltzer Avenue 8,243.23 feet to a point of intersection with the compromise line between the Bolsa Chica and Los Alamitos Ranchos; thence in a northeasterly direction with the compromise line between the Bolsa Chica and Los Alamitos Ranchos to a point of intersection with the center line of Bolsa Chica Road, said center line extending N. 0° 24' 05" W., 7,309.42 feet from its point of intersection with the center line of Smeltzer Avenue; thence S. 0° 24' 05" E., with the center line of Bolsa Chica Avenue 7,309.42 feet to the point of intersection with the center line of Smeltzer Avenue the point of beginning.

AREA No. 3

Beginning at the most northeasterly corner of a parcel of land conveyed by Alamitos Land Company, a corporation, to George B. Arvanitis by Deed recorded January 17, 1944, in Book 1224, page 539, official records of Orange County, California, and as shown in Book 14, page 36, record of Survey of said county, said point of beginning also being in the northerly line of Tide Land Location No. 141, as recorded in Book 1, page 194 of Patents, records of said county, said corner also being identified as the most northerly corner of Parcel 174-2 in Case No. 3436-RJ Civil, instituted by the United States to acquire lands for the Naval Ammunition and Net Depot, Seal Beach, California, thence S. 37° 17' 13" W., 592.26 feet to a point in the northeasterly line of former California State Highway; thence southeasterly along the arc of a curve, having a radius of 1,350 feet, 211.73 feet to a line tangent; thence continuing along the northeasterly line of former California State Highway S. 52° 58' 07" E., 18.29 feet to a tangent curve having a radius of 1,350 feet; thence along said curve for an arc distance of 759.33 feet; thence S. 40° 31' 53" W., leaving the northeasterly line of former California State Highway, for a distance of 88.09 feet to the northeasterly right-of-way line of the Pacific Electric Railway; thence in a northwesterly direction along the northeasterly right-of-way line of said Pacific Electric Railway, a distance of 450.51 feet, said northeasterly right-of-way line of said Pacific Electric Railway being an arc of a circle, convex northeasterly having a radius of 5,754.60 feet, the long chord of said arc of a circle forming an angle of 94° 17' 01" (measured from northeasterly to north to northwesterly) with the last described radial line; thence in a southwesterly direction along a radial line, said radial line being at right angles to the tangent to the last mentioned arc at said point, to its intersection with the southwesterly right-of-way line of said Pacific Electric Railway, a distance of 50 feet more or less; thence in a northwesterly direction along said southwesterly right-of-way line of said Pacific Electric Railway, a distance of 738.00 feet more or less to its intersection with the extension northeasterly of the southeasterly line of Lots 45 and 119 in locks "C" and "B" respectively in "Surf Side Colony" Phillips and Hambaugh Realty Construction Corporation Subdivision, as recorded in Book 4 of Maps, pages 4, 5 and 6, in the Recorder's Office of Orange County, said southwesterly right-of-way line of said Pacific Electric Railway being an arc of a circle, convex northeasterly and having a radius of 5,704.6 feet the long chord of said arc of a circle having an angle of 88° 17' 36.6" (as measured from southwesterly to west to northwesterly) with the last mentioned radial line; thence in a southwesterly direction along the extension northeasterly of the southeasterly line of Lots 45 and 119 and the southeasterly line of said Lots to the southeasterly corner of the aforementioned Lot 119, a distance of 90.10 feet more or less; thence in a northwesterly direction along the southwesterly line of said Lot 119 to its intersection with the extension northeasterly of the southeasterly line of Lot 120 in Block "A" in said "Surf Side Colony" a distance of 11.41 feet more or less; thence in a southwesterly direction along the extension northeasterly of said southeasterly line of said Lot 120 and the southeasterly line of said Lot to the Ordinary High Tide Line of the Pacific Ocean; thence in a general northerly and northwesterly direction with the Ordinary High Tide Line of the Pacific Ocean 4,000 feet more or less; thence in a general northerly, northeasterly and southeasterly direction following the Ordinary High Tide Line of the Pacific Ocean and Anaheim Bay for a distance of 4,700 feet more or less to a point of intersection with the North and South center line of Section 13, T. 5 N., R. 12 W. and a line extended northwesterly with a bearing of N. 87° 30' 07" W., for a distance of 800 feet, more or less from the point of beginning of this description; thence following said line S. 87° 30' 07" E., 800 feet more or less to the point of beginning.

AREA No. 4

Starting at a point on the northerly line of Bolsa Avenue, 387.25 feet westerly of the North and South center line of Section 12, T. 5 S., R. 12 W., thence N. 0° 11' 19" E., 1,020 feet; thence N. 89° 48' 41" W., 136.8 feet to the Point of Beginning of this description; thence S. 31° 24' 53" W., 121.91 feet; thence N. 0° 11' 19" E., 102.24 feet; thence S. 89° 48' 41" E., 63.2 feet to the point of beginning.

AREA No. 5

A strip of land 100 feet in width being a portion of Lot "C-2" of the Partition of the Rancho Los Alamitos according to Plat of the Rancho Los Alamitos filed in Case No. 13527 of the Superior Court of the County of Los Angeles, State of California, said strip of land being 50 feet on each side of the following described center line:

Beginning at Railway Survey Station 1320+03 of the surveyed center line of the Pacific Electric Railway as shown on Plat "B" attached to said deed and made a part thereof; said Station being in the boundary line between Lot "B-2" and said Lot "C-2" according to said Plat in Case No. 13527 aforesaid and South 31° 17' West 1,224.58 feet a little more or less from the most easterly corner of said Lot "B-2"; thence from said point of beginning South 42° 24' East 953.6 feet to Railway Survey Station 1329+61.6 of the surveyed center line of the Pacific Electric Railway as shown on the above mentioned Plat "B" said last mentioned Station being in Course No. 42 of the Survey of the Rancho Los Alamitos made under instructions of the Survey General of the United States by Deputy Surveyor G. H. Thompson November 28, 1873, and recorded in Record of Patents of Los Angeles County, California, in Book 1, page 453; said Course No. 42 being part of the Southern boundary line of said Lot "C-2" and said Railway Survey Station 1329+61.6 being South 57° 00' West 301.75 feet, a little more or less, from Station No. 42 of the above mentioned survey of the Rancho Los Alamitos.

Excepting therefrom that portion thereof lying northwesterly of the southwesterly prolongation of the southeasterly line of Bay Boulevard as recorded in Book 554, page 318 of Deeds, Records of Orange County.

AREA NO. 6

All that portion of the southwest quarter of Section 13, T. 5 S., R. 12 W., contained within Lots 6, 7 and 8, Tide Land Survey No. 3 as recorded in Miscellaneous Map Book 27, pages 23 and 24 of Official Records of Orange County, California.

Excluding therefrom any portion of the following described parcel lying within the said southwest quarter of Section 13, T. 5 S., R. 12 W., described as follows:

A parcel of land in Section 13, T. 5 S., R. 12 W., SBB&M, in Orange County, California, within Tract No. 893 as shown in Book 27, pages 23 and 24, Miscellaneous Maps of said Orange County, and within the limits of that certain parcel of land acquired by the United States under Condemnation Case 3436-WM Civil in the District Court of the United States in and for the Southern District of California, Central Division, more particularly described as follows:

Beginning at the common corner of Sections 12 and 13, T. 5 S., R. 12 W. and Sections 7 and 18, T. 5 S., R. 11 W; thence westerly along the north line of said Section 13, 1,647 feet; thence southerly and parallel to the east line of said Section 13, 693 feet; to the true point of beginning: Thence easterly and parallel to the north line of said Section 13, 1,000 feet; thence southerly and parallel to the east line of said Section 13, 2,000 feet; thence westerly and parallel to the north line of said Section 13 to the northeasterly right-of-way line of the California State Highway (U. S. 101) as shown in Deed recorded in Book 1537, page 319, Official Records of said Orange County; thence 70 feet along the arc of a curve concave to the southwest, having a radius of 2,150 feet, said arc forming a part of the northeasterly right-of-way line of said California State Highway (U. S. 101); thence leaving said northeasterly right-of-way line northeasterly in a straight line to the true point of beginning, containing 75.9 acres more or less.

2. The Secretary of the Interior shall take such action as may be necessary to protect the United States from loss on account of drainage or threatened drainage of oil and gas from such lands.

3. The jurisdiction of the Department of the Interior over such lands shall be subject to the primary jurisdiction of the Department of the Navy over the lands for naval purposes.

4. Prior to any advertisement for bids to lease any of the lands mentioned herein, the Department of the Navy shall have the opportunity to indicate the further reservations and restrictions that are to be included in the proposed lease or leases.

5. All moneys received as royalties under leases, or otherwise, on account of oil and gas extracted from such lands shall be paid into the Treasury of the United States and credited to miscellaneous receipts.

ORME LEWIS,
Assistant Secretary of the Interior

AUGUST 8, 1955.

[F. R. Doc. 55-6562; Filed, Aug. 11, 1955; 8:46 a. m.]

PROPOSED RULE MAKING

DEPARTMENT OF THE TREASURY

Internal Revenue Service

[26 CFR (1954) Part 1]

INCOME TAX: TAXABLE YEARS BEGINNING AFTER DEC. 31, 1953; PARTNERSHIPS

NOTICE OF PROPOSED RULE MAKING

Notice is hereby given, pursuant to the Administrative Procedure Act, approved June 11, 1946, that the regulations set forth in tentative form below are proposed to be prescribed by the Commissioner of Internal Revenue with the approval of the Secretary of the Treasury. Prior to final adoption of such regulations, consideration will be given to any data, views, or arguments pertaining thereto which are submitted in writing, in duplicate, to the Commissioner of Internal Revenue, Attention: T:P Washington 25, D. C., within the period of 30 days from the date of publication of this notice in the FEDERAL REGISTER. The proposed regulations are to be issued under the authority contained in sections 702, 704, 705, 706, 732, 736, 743, 751, 754, 755, 761, 771, and 7805 of the Internal Revenue Code of 1954 (68A Stat. 239, 240, 242, 246, 248, 249, 250, 251, 252, 253, and 917)

[SEAL] T. COLEMAN ANDREWS,
Commissioner of Internal Revenue.

The following regulations relating to partners and partnerships are hereby prescribed under subchapter K of chapter 1 of the Internal Revenue Code of 1954:

PARTNERS AND PARTNERSHIPS

DETERMINATION OF TAX LIABILITY

§ 1.701 *Statutory provisions; partners, not partnership, subject to tax.*

SEC. 701. *Partners, not partnership, subject to tax.* A partnership as such shall not be subject to the income tax imposed by this chapter. Persons carrying on business as partners shall be liable for income tax only in their separate or individual capacities.

§ 1.701-1 *Partners, not partnership, subject to tax*—(a) *In general.* Partners are liable for income tax only in their separate capacities. Partnerships as such are not subject to the income tax imposed by subtitle A but are required to make returns of income under the provisions of section 6031. For definition of the terms "partner" and "partnership," see section 761 and § 1.761-1.

(b) *Partnership returns.* Every partnership shall make a return for each taxable year. The return shall state specifically the items of partnership gross income and the deductions allowable by subtitle A or, in the case of certain unincorporated organizations described in § 1.761-1 (b) such information as is required under that section. The return shall be made on Form 1065 and shall contain the information required by the form or instructions issued with respect thereto. Such return shall be made for the taxable year of the partnership, irrespective of the taxable years of the partners. For taxable years of a partnership and a partner, see section 706 (b) and § 1.706-1 (b) See section 703 and § 1.703-1 for partnership computations. The partnership return shall include the names and addresses of the persons who are entitled to share in the partnership income or loss and the amount of the distributive share of each such person, whether or not distributed. The return shall be signed by any one of the partners. The fact that a partner's name is signed on the return shall be prima facie evidence that such partner is authorized to sign the return on behalf of the partnership. See section 6063.

§ 1.702 *Statutory provisions; income and credits of partner*

SEC. 702. *Income and credits of partner*—(a) *General rule.* In determining his income tax, each partner shall take into account separately his distributive share of the partnership's—

(1) Gains and losses from sales or exchanges of capital assets held for not more than 6 months,

(2) Gains and losses from sales or exchanges of capital assets held for more than 6 months,

(3) Gains and losses from sales or exchanges of property described in section 1231 (relating to certain property used in a trade or business and involuntary conversions),

(4) Charitable contributions (as defined in section 170 (c)),

(5) Dividends with respect to which there is provided a credit under section 34, an exclusion under section 116, or a deduction under part VIII of subchapter B,

(6) Taxes, described in section 901, paid or accrued to foreign countries and to possessions of the United States,

(7) Partially tax-exempt interest on obligations of the United States or on obligations of instrumentalities of the United States as described in section 35 or section 242 (but, if the partnership elects to amortize the premiums on bonds as provided in section 171, the amount received on such obligations shall be reduced by the reduction provided under section 171 (a) (3)),

(8) Other items of income, gain, loss, deduction, or credit, to the extent provided by regulations prescribed by the Secretary or his delegate, and

(9) Taxable income or loss, exclusive of items requiring separate computation under other paragraphs of this subsection.

(b) *Character of items constituting distributive share.* The character of any item of income, gain, loss, deduction, or credit included in a partner's distributive share under paragraphs (1) through (8) of subsection (a) shall be determined as if such item were realized directly from the source from which realized by the partnership, or incurred in the same manner as incurred by the partnership.

(c) *Gross income of a partner.* In any case where it is necessary to determine the gross income of a partner for purposes of this title, such amount shall include his distributive share of the gross income of the partnership.

§ 1.702–1 *Income and credits of partner*—(a) *General rule.* Each partner is required to take into account separately in his return his distributive share, whether or not distributed, of each class of partnership income, gain, loss, deduction, or credit described in subparagraphs (1) to (9) inclusive. For the taxable year of inclusion in his taxable income of a partner's distributive share of partnership taxable income, see section 706 (a) and § 1.706–1 (a) Such distributive share shall be determined as provided in section 704 and § 1.704–1. Accordingly, in determining his income tax:

(1) Each partner shall take into account, as part of his gains and losses from sales or exchanges of capital assets held for not more than six months, his distributive share of the combined net amount of such gains and losses of the partnership.

(2) Each partner shall take into account, as part of his gains and losses from sales or exchanges of capital assets held for more than six months, his distributive share of the combined net amount of such gains and losses of the partnership.

(3) Each partner shall take into account, as part of his gains and losses from sales or exchanges of property described in section 1231 (relating to certain property used in trade or business and involuntary conversions) his distributive share of the combined net amount of such gains and losses of the partnership. (The partnership shall not combine such items with items set forth in (1) or (2) above.)

(4) Each partner shall take into account, as part of the charitable contributions paid by him, his distributive share of the total charitable contributions paid by the partnership within the partnership's taxable year. Section 170 determines the extent to which such amount may be allowed as a deduction to the partner. For the definition of the term "charitable contribution", see section 170 (c)

(5) Each partner shall take into account, as part of the dividends received by him from domestic corporations, his distributive share of dividends received by the partnership, with respect to which the partner is entitled to a credit under section 34, an exclusion under section 116, or a deduction under part VIII of subchapter B.

(6) Each partner shall take into account, as part of his taxes described in section 901 which have been paid or accrued to foreign countries or to possessions of the United States, his distributive share of such taxes which have been paid or accrued by the partnership, according to its method of accounting. A partner may elect to treat the total amount of such taxes paid or accrued by him, including his distributive share of such taxes of the partnership, as a deduction under section 164 or as a credit under section 901, subject to the provisions of sections 901–905, inclusive.

(7) Each partner shall take into account, as part of the partially tax-exempt interest received by him on obligations of the United States or on obligations of instrumentalities of the United States, as described in section 35 or section 242, his distributive share of such partially tax-exempt interest received by the partnership. However, if the partnership elects to amortize premiums on bonds as provided in section 171, the amount received on such obligations by the partnership shall be reduced by the amortizable bond premium applicable to such obligations as provided under section 171 (a) (3)

(8) (i) Each partner shall take into account separately, as part of any class of income, gain, loss, deduction, or credit, his distributive share of any partnership item of the same class which would affect the computation of his income tax. Examples of items which should be accounted for separately are: (*a*) amounts recovered with respect to bad debts, prior taxes, and delinquency amounts (section 111) (*b*) exploration expenditures (section 615) (*c*) soil and water conservation expenditures (section 175) (*d*) gains and losses from wagering transactions (section 165 (d)) (*e*) "hobby losses" (section 270) and (*f*) any items or class of items of income, gain, loss, deduction, or credit subject to a special allocation under the partnership agreement differing from the allocation of partnership taxable income or loss generally (section 704 (b) and § 1.704–1 (b))

(ii) Each partner shall aggregate the amount of his separate deductions or exclusions and his distributive share of partnership deductions or exclusions in determining the amount allowable to him of any deduction or exclusion under subtitle A as to which a limitation is imposed. For example, partner A has individual exploration expenditures of $75,000. He is also a member of the AB partnership which has exploration expenditures of $120,000 of which $100,000 is allowed as a deduction which must be accounted for separately. A's distributive share of this item is $50,000. However, the total amount that A can deduct as exploration expenditures under section 615 (a) is also limited to $100,000. Therefore, the excess of $25,000 ($125,000—$100,000) is not deductible by A.

(iii) Each partner shall take into account as part of any itemized deductions allowable to him under part VII of subchapter B, his distributive share of any expenditure of the partnership which would constitute an allowable deduction under that part when incurred by an individual, if the expenditure is not otherwise deductible by the partnership as a business expense.

(iv) Each partner shall take into account, for the purpose of determining the net operating loss deduction under section 172, his distributive share of the income and loss of the partnership in computing his net operating loss or his taxable income (where required to be computed in accordance with section 172 (d)) with the following modifications:

(*a*) *Long-term capital gains and losses.* The partner's distributive share of partnership gains and losses from sales or exchanges of capital assets held for more than six months shall be taken into account in full. The gains and losses from sales or exchanges of capital assets attributable to the trade or business held for more than six months shall be segregated from gains and losses from sales or exchanges of capital assets not attributable to the trade or business.

(*b*) *Short-term capital gains and losses.* The partner's distributive share of partnership gains and losses from sales or exchanges of capital assets attributable to the trade or business and held for not more than six months, and the gains and losses from sales or exchanges of capital assets not attributable to the trade or business, shall be segregated.

(*c*) *Gains and losses from sales or exchanges of certain property used in a trade or business and involuntary conversions.* The partner's distributive share of partnership gains and losses from sales, exchanges, or involuntary conversions of certain property used in a trade or business, as defined in section 1231 (b) (1), shall be segregated from his distributive share of partnership gains and losses from the involuntary conversion of capital assets held for more than six months.

(*d*) *Other items affecting computation of partner's separate income tax.* The partner's distributive share of any other item of income, gain, loss, or deduction of a partnership attributable to its trade or business, other than those described in subdivisions (*a*) (*b*) and (*c*) above, which will affect the computation of the partner's income tax, is required to be stated separately by the partner and shall be segregated from the partner's distributive share of items of similar character not attributable to the trade or business.

(*e*) *Ordinary taxable income or loss.* (*1*) After excluding all items required to be segregated by subdivisions (*a*) to (*d*) inclusive, of this subdivision, there shall be computed—

(*i*) A business ordinary income of the partnership, which shall consist of the excess of the business gross income over the business deductions; or

(*ii*) A business ordinary net loss of the partnership, which shall consist of the excess of the business deductions over the business gross income; and

(*iii*) A nonbusiness ordinary income of the partnership, which shall consist of the excess of the nonbusiness gross income over the nonbusiness deductions; or

(*iv*) A nonbusiness ordinary net loss of the partnership, which shall consist of the excess of the nonbusiness deductions over the nonbusiness gross income.

(2) Each partner's distributive share of business ordinary income of the partnership shall be taken into account by him as business ordinary income, and his distributive share of a business ordinary net loss of the partnership as a business ordinary deduction. Each partner's distributive share of nonbusiness ordinary income of the partnership shall be taken into account by him as nonbusiness

ordinary income, and his distributive share of a nonbusiness ordinary net loss of the partnership as a nonbusiness ordinary deduction.

(9) Each partner is also required to include in his return his distributive share of the taxable income or loss of the partnership, exclusive of items requiring separate computations under subparagraphs (1) to (8), inclusive. For limitation on allowance of a partner's distributive share of partnership losses, see section 704 (d) and § 1.704–1 (d)

(b) *Character of items constituting distributive share.* The character in the hands of a partner of any item of income, gain, loss, deduction, or credit described in section 702 (a) (1) to (8) inclusive, shall be determined as if such item were realized directly from the source from which realized by the partnership or incurred in the same manner as incurred by the partnership. For example, a partner's distributive share of gain from the sale of depreciable property used in the trade or business of the partnership shall be considered as gain from the sale of such depreciable property in the hands of the partner. Similarly, a partner's distributive share of partnership "hobby losses" (section 270) retains its character as a "hobby loss" in the hands of the partner.

(c) *Gross income of a partner* (1) Where it is necessary to determine the gross income of a partner, such gross income shall include the partner's distributive share of the gross income of the partnership, that is, the amount of gross income of the partnership from which the partner's distributive share of partnership taxable income or loss (including items described in section 702 (a) (1) to (8), inclusive) was derived. For example, a partner is required to include his distributive share of partnership gross income:

(i) In computing his gross income for the purpose of determining the necessity of filing a return (section 6012 (a))

(ii) In determining the application of the provision permitting the spreading of income for services rendered over a 36-month period (section 1301) and

(iii) In computing the amount of gross income received from sources within possessions of the United States (section 931)

(2) In determining the applicability of the 6-year period of limitation provided in section 6501 (e) (relating to omission of more than 25 percent of gross income) a partner's gross income includes his distributive share of partnership gross income. In this respect, the amount of partnership gross income from which the partner's distributive share of partnership taxable income or loss (as shown on the partner's return) was derived is considered as an amount of gross income shown on the return for the purposes of section 6501 (e)

(3) Where a partnership engaged in the business of farming adopts the method described in section 175 (a) of treating soil and water conservation expenditures, a partner shall include his share of partnership gross income from farming in determining his gross income from farming for purposes of applying the limitations of section 175 (b)

(d) *Partners in community property States.* If separate returns are made by a husband and wife domiciled in a community property State, and only one spouse is a member of the partnership, the part of his or her distributive share of any item or items listed in paragraph (a) (1) to (9) inclusive, which is community property, or which is derived from community property, should be reported by the husband and wife in equal proportions.

§ 1.703 *Statutory provisions; partnership computations.*

SEC. 703. *Partnership computations*—(a) *Income and deductions.* The taxable income of a partnership shall be computed in the same manner as in the case of an individual except that—

(1) The items described in section 702 (a) shall be separately stated, and

(2) The following deductions shall not be allowed to the partnership:

(A) The standard deduction provided in section 141,

(B) The deductions for personal exemptions provided in section 151,

(C) The deduction for taxes provided in section 164 (a) with respect to taxes, described in section 901, paid or accrued to foreign countries and to possessions of the United States,

(D) The deduction for charitable contributions provided in section 170,

(E) The net operating loss deduction provided in section 172, and

(F) The additional itemized deductions for individuals provided in part VII of subchapter B (sec. 211 and following).

(b) *Elections of the partnership.* Any election affecting the computation of taxable income derived from a partnership shall be made by the partnership, except that the election under section 901, relating to taxes of foreign countries and possessions of the United States, shall be made by each partner separately.

§ 1.703–1 *Partnership computations*—(a) *Income and deductions.* (1) The taxable income of a partnership shall be computed in the same manner as the taxable income of an individual, except as otherwise provided in this section. A partnership is required to state separately in its return the items described in section 702 (a) (1) to (7) inclusive and, in addition, those items described in section 702 (a) (8) which the partner is required to take into account separately in determining his income tax. See § 1.702–1 (a) (8) The partnership is further required to compute and to state separately in its return:

(i) As taxable income, the total of all other items of gross income (not separately stated) over the total of all other allowable deductions (not separately stated) or

(ii) As loss, the total of all other allowable deductions (not separately stated) over the total of all other items of gross income (not separately stated)

The taxable income or loss so computed shall be accounted for by the partners in accordance with their distributive shares as provided in section 702 (a) (9)

(2) The partnership is not allowed the following deductions:

(i) The standard deduction provided in section 141.

(ii) The deduction for personal exemptions provided in section 151.

(iii) The deduction provided in section 164 (a) for taxes described in section 901 paid or accrued to foreign countries or possessions of the United States. Each partner's distributive share of such taxes shall be accounted for separately by him as provided in section 702 (a) (6) and § 1.702–1 (a) (6).

(iv) The deduction for charitable contributions provided in section 170. Each partner is considered as having paid within his taxable year his distributive share of any contribution or gift, payment of which was made by the partnership within its taxable year ending within or with the partner's taxable year. This item shall be accounted for separately by the partners as provided in section 702 (a) (4) and § 1.702–1 (a) (4)

(v) The net operating loss deduction provided in section 172.

(vi) The additional itemized deductions for individuals provided in part VII of subchapter B as follows:

(*a*) Expenses for production of income (section 212),

(*b*) Medical, dental, etc., expenses (section 213),

(*c*) Expenses for the care of certain dependents (section 214),

(*d*) Alimony, etc., payments (section 215), and

(*e*) Amounts representing taxes and interest paid to a cooperative housing corporation (section 216)

(vii) The deduction for capital gains provided by section 1202 and the deduction for capital loss carryover provided by section 1212.

(b) *Election of the partnership*—(1) *General rule.* Any elections (other than the election with respect to foreign taxes) affecting the computation of income derived from a partnership shall be made by the partnership. For example, elections of methods of accounting, methods of computing depreciation, and methods of treating soil and water conservation expenditures and exploration expenditures shall be made by the partnership rather than by the partners separately. All partnership elections are applicable to all partners equally but any election made by a partnership shall have no force or effect with respect to any partner's nonpartnership interests.

(2) *Exception.* Each partner shall add his distributive share of taxes described in section 901 paid or accrued by the partnership to foreign countries or possessions of the United States to any such taxes paid or accrued by him, and may elect to use the total amount either as a credit against tax or as a deduction from income.

§ 1.704 *Statutory provisions; partner's distributive share.*

SEC. 704. *Partner's distributive share*—(a) *Effect of partnership agreement.* A partner's distributive share of income, gain, loss, deduction, or credit shall, except as otherwise provided in this section, be determined by the partnership agreement.

(b) *Distributive share determined by income or loss ratio.* A partner's distributive share of any item of income, gain, loss, deduction, or credit shall be determined in accordance with his distributive share of taxable income or loss of the partnership,

as described in section 702 (a) (9), for the taxable year, if—

(1) The partnership agreement does not provide as to the partner's distributive share of such item, or

(2) The principal purpose of any provision in the partnership agreement with respect to the partner's distributive share of such item is the avoidance or evasion of any tax imposed by this subtitle.

(c) *Contributed property*—(1) *General rule.* In determining a partner's distributive share of items described in section 702 (a), depreciation, depletion, or gain or loss with respect to property contributed to the partnership by a partner shall, except to the extent otherwise provided in paragraph (2) or (3), be allocated among the partners in the same manner as if such property had been purchased by the partnership.

(2) *Effect of partnership agreement.* If the partnership agreement so provides, depreciation, depletion, or gain or loss with respect to property contributed to the partnership by a partner shall, under regulations prescribed by the Secretary or his delegate, be shared among the partners so as to take account of the variation between the basis of the property to the partnership and its fair market value at the time of contribution.

(3) *Undivided interests.* If the partnership agreement does not provide otherwise, depreciation, depletion, or gain or loss with respect to undivided interests in property contributed to a partnership shall be determined as though such undivided interests had not been contributed to the partnership. This paragraph shall apply only if all the partners had undivided interests in such property prior to contribution and their interests in the capital and profits of the partnership correspond with such undivided interests.

(d) *Limitation on allowance of losses.* A partner's distributive share of partnership loss (including capital loss) shall be allowed only to the extent of the adjusted basis of such partner's interest in the partnership at the end of the partnership year in which such loss occurred. Any excess of such loss over such basis shall be allowed as a deduction at the end of the partnership year in which such excess is repaid to the partnership.

(e) *Family partnerships*—(1) *Recognition of interest created by purchase or gift.* A person shall be recognized as a partner for purposes of this subtitle if he owns a capital interest in a partnership in which capital is a material income-producing factor, whether or not such interest was derived by purchase or gift from any other person.

(2) *Distributive share of donee includible in gross income.* In the case of any partnership interest created by gift, the distributive share of the donee under the partnership agreement shall be includible in his gross income, except to the extent that such share is determined without allowance of reasonable compensation for services rendered to the partnership by the donor, and except to the extent that the portion of such share attributable to donated capital is proportionately greater than the share of the donor attributable to the donor's capital. The distributive share of a partner in the earnings of the partnership shall not be diminished because of absence due to military service.

(3) *Purchase of interest by member of family.* For purposes of this section, an interest purchased by one member of a family from another shall be considered to be created by gift from the seller, and the fair market value of the purchased interest shall be considered to be donated capital. The "family" of any individual shall include only his spouse, ancestors, and lineal descendants, and any trusts for the primary benefit of such persons.

§ 1.704–1 *Partner's distributive share*—(a) *Effect of partnership agreement.* A partner's distributive share of any item or class of items of income, gain, loss, deduction, or credit of the partnership shall be determined by the partnership agreement unless otherwise provided in this section. For definition of partnership agreement, see section 761 (c) and § 1.761–1 (d)

(b) *Distributive share determined by income or loss ratio.* (1) If the partnership agreement makes no specific provision for the manner of sharing one or more items or classes of items, each partner's distributive share of such item or class of items shall be determined in accordance with the partnership agreement with respect to taxable income or loss, as described in section 702 (a) (9) If the partnership agreement provides a different ratio for sharing income from that applicable for sharing losses, the income ratio shall be applicable if the partnership has taxable income exclusive of items requiring separate computation under section 702 (a) (1) to (8), inclusive, in the particular taxable year, and the loss ratio shall be applicable in any year in which there is a loss exclusive of items requiring separate computation under section 702 (a) (1) to (8), inclusive.

(2) If the principal purpose of any provision in the partnership agreement with respect to a partner's distributive share of a particular item or class of items is to avoid or evade the Federal income tax, the partner's distributive share of that item or class of items shall be redetermined in accordance with the income or loss ratio prescribed in the partnership agreement with respect to taxable income or loss, as described in section 702 (a) (9) However, where a provision in a partnership agreement for a special allocation of a certain item or class of items is not a device for reducing taxes of certain partners and has substantial economic effect, then such a provision will be recognized for tax purposes. In determining whether the principal purpose of any provision in the partnership agreement for a special allocation is the avoidance or evasion of Federal income tax, each such provision must be considered on its own merits in relation to all the surrounding facts and circumstances. The presence or absence of substantial economic effect in the special allocation provided for in the agreement is only one of the facts and circumstances to be considered. The application of the provisions of this subparagraph may be illustrated by the following examples:

Example (1). The provisions of a partnership agreement allocate all partnership loss on the sale of depreciable property used in the trade or business to one partner who has no such gains individually. An equivalent amount of partnership loss or deduction of a different character is allocated to other partners who individually have gains from the sale of depreciable property used in the trade or business. Such an allocation will not be recognized, and under section 704 (b) (2) those items will be allocated to all the partners in accordance with the provisions of the partnership agreement for sharing partnership income or loss generally.

Example (2). The provisions of a partnership agreement allocate to a partner who is a resident of Puerto Rico a percentage of the income derived from sources within Puerto Rico which is greater than his distributive share of partnership income generally. If the primary purpose of this allocation is to encourage Puerto Rican transactions, it may be considered as having substantial economic effect rather than being a device to reduce the taxes of certain partners.

Example (3). Rather than impair the credit standing of the AB partnership by a distribution, the partners agree to invest surplus partnership funds in an equal dollar amount of municipal bonds and corporate stock. The partners further agree that A is to receive all the interest income from tax-exempt bonds and B is to receive all the dividend income from corporate stock. Such an allocation may be recognized unless it is a device for the allocation of tax-exempt interest without having substantial economic effect on either partner's share of the total partnership income. On the other hand, under an agreement with respect to partnership CD, it is provided that C's distributive share of income shall be the first $10,000 of tax-exempt income, and D's distributive share of income shall be the first $10,000 of dividend income, the balances to be divided equally. Where this purpose is to allocate tax-exempt interest to C who has substantial income from other sources and where the allocation does not have any real economic effect, it will be disregarded and each partner's distributive share will then be allocated in accordance with the provisions of the partnership agreement for sharing partnership income or loss generally.

(c) *Contributed property*—(1) *In general.* Where property has been contributed by a partner to a partnership, section 704 (c) and this paragraph provide rules for determining a partner's distributive share of depreciation, depletion, or gain or loss with respect to such contributed property. These rules provide certain alternatives in determining the partners' distributive shares of such items in order to account for precontribution appreciation or diminution in value of the property contributed. When the partnership agreement is silent as to the treatment of such items with respect to contributed property (and if such property is not an undivided interest as described in section 704 (c) (3)), depreciation, depletion, or gain or loss arising with respect to such property shall be treated in the same manner as though such items arose with respect to property purchased by the partnership. The application of this provision may be illustrated by the following examples:

Example (1). A and B form an equal partnership. A contributes $1,000 cash and B contributes stock with an adjusted basis to him of $400 and a fair market value of $1,000. Under section 723, the basis of the stock to the partnership is also $400. One year later, the stock is sold for $1,200. There is no provision in the partnership agreement for treatment of items with respect to contributed property. Under section 704 (c) (1), the $800 gain on the sale of the stock is treated as if it were gain on property that had been purchased by the partnership and subsequently sold. Therefore, each partner's distributive share of such gain is $400.

Example (2). C and D form an equal partnership. C contributes machinery worth $10,000 with an adjusted basis to him of $4,000. D contributes $10,000 cash. Under the provisions of section 722, the basis of A's

partnership interest is $4,000 and the basis of B's interest is $10,000. There is no provision in the partnership agreement relating to contributed property. If the contributed property depreciates at an annual rate of 10 percent, the partnership will have an annual depreciation deduction of $400, which will result in a reduction of $200 in each partner's distributive share of partnership income. Thus, at the end of the first year, the adjusted basis of the contributed property will be $3,600. If the partnership has no other taxable income or loss for that year, each partner will have a deduction of $200 representing his distributive share of partnership loss for the year. C's adjusted basis for his interest will be $3,800 ($4,000, the original basis of his interest, reduced by $200) D's adjusted basis will be $9,800 ($10,000, reduced by $200).

Example (3). Assume that the property in example (2) is sold in the second year of partnership operation for $9,000. The partnership gain will be $5,400 ($9,000, the amount realized, less the adjusted basis of $3,600). Each partner's share of the $5,400 gain will be $2,700. If we assume that the partnership has no other taxable income or loss for that year, each partner will have a capital gain from the partnership of $2,700, representing his distributive share of gain from the sale of property used in the partnership business. C's adjusted basis for his interest will then be $6,500 (the basis of $3,800, increased by the gain of $2,700). D's adjusted basis will be $12,500 (the basis of $9,800 increased by the gain of $2,700). If the partnership is then terminated, and its assets consisting of $19,000 in cash are distributed to the partners pro rata in liquidation of their entire interests, C will have a capital gain of $3,000 ($9,500, the amount received, less $6,500, the adjusted basis of his interest). D will have a capital loss of $3,000 (D's adjusted basis, $12,500, reduced by the amount received, $9,500).

(2) *Effect of partnership agreement.* (i) If the partners so provide in the partnership agreement, depreciation, depletion, or gain or loss with respect to contributed property may be allocated among the partners in a manner which takes into account all or any part of the difference between the adjusted basis and the fair market value of contributed property at the time of contribution. The appreciation or diminution in value represented by the difference between the adjusted basis and the fair market value of contributed property at the time of contribution may thus be attributed to the contributing partner upon a subsequent sale or exchange of the property by the partnership. Such appreciation or diminution may also be used to determine the amount of depreciation or depletion with respect to such property allowable to the contributing partner and the noncontributing partners. In any case, however, the total depreciation, depletion, or gain or loss allocated to the partners is limited to a "ceiling" which cannot exceed the amount of gain or loss realized by the partnership or the depreciation or depletion allowable to it. The difference between the adjusted basis and the fair market value represents a deferred gain or loss to the contributing partner which is realized by him either when such property is sold or which is, in substance, realized by him in that he does not receive annual deductions for depreciation or depletion with respect to the property contributed. The application of this subdivision may be illustrated by the following examples:

Example (1). Assume that partners C and D, in examples (2) and (3) under subparagraph (1), agree under section 704 (c) (2) to attribute to C, the contributor of the machinery, the potential gain of $6,000 represented by the difference between its adjusted basis of $4,000 and its fair market value of $10,000. With his contribution of $10,000 in cash D has, in effect, purchased an undivided half interest in the property for $5,000. Since the property depreciates at an annual rate of 10 percent, D would be entitled to a depreciation deduction of $500 per year. However, since under the "ceiling" approach the partnership is allowed only $400 per year (10 percent of $4,000), no more than $400 may be allocated between the partners. Therefore, the $400 deduction for depreciation is allocated entirely to D and none to C, the contributor. At the end of the first year, the adjusted basis of the contributed property will be $3,600. Since the $400 deduction is allocated entirely to D, if the partnership has no other taxable income or loss, C will have no income or loss, and D will have a deduction of $400. C's basis for his interest will remain $4,000. D's adjusted basis for his interest will be $9,600 ($10,000, the original basis of his interest, reduced by the deduction of $400).

Example (2). Assume that the partners in example (1) agree under section 704 (c) (2) that, upon a sale of the contributed property, the portion of the proceeds attributable to the excess of the fair market value of the property at date of contribution (less accumulated depreciation) over its basis at date of contribution (less accumulated depreciation) shall result in gain to the contributing partner only. If the property is sold in the second year of partnership operation for $9,000, the partnership gain of $5,400 ($9,000, the amount realized, less the basis of $3,600) must be allocated to the partners under the terms of the agreement. The fair market value of the property as depreciated is $9,000 ($10,000, the value on contribution, less $1,000, the accumulated depreciation). Under section 704 (c) (2) and the terms of the parnership agreement, the difference between $9,000, the fair market value as depreciated, and $3,600, the adjusted basis of the property, or $5,400, represents the portion of the gain to be allocated to C. None of the gain is allocated to D. (If the property were sold for more than $9,000, the portion of the gain in excess of $5,400 would be divided equally between the partners in accordance with their agreement for sharing gains. If the property were sold for less than $9,000, the entire gain would be allocated to C and nothing to D.) If we assume that the partnership engaged in no other transactions that year, C will report a capital gain of $5,400, and D, no income or loss. C's adjusted basis for his interest will then be $9,400 ($4,000, his original basis, increased by the gain of $5,400). D's adjusted basis will be $9,600 ($10,000, his original basis, less $400 depreciation deduction in the first partnership year). If the partnership is then liquidated, and its assets consisting of $19,000 in cash distributed to the partners pro rata, C will have a capital gain of $100 ($9,500, the amount received, less $9,400, the adjusted basis of his interest). D will have a capital loss of $100 (the excess of D's adjusted basis, $9,600, over the amount received, $9,500).

(ii) For the effect of an agreement under section 704 (c) (2) on undivided interests in property contributed to the partnership where the partners' interests in the capital and profits of the partnership do not correspond with such undivided interests, see § 1.704-1 (c) (3) (ii)

(3) *Undivided interests.* (i) Section 704 (c) (3) provides a special rule for the allocation of depreciation, depletion, or gain or loss with respect to undivided interests in property contributed by the partners to a partnership were the partnership agreement does not provide otherwise. This provision applies only to property contributed to a partnership by all of its partners and only where the relative undivided interests of the partners in the property prior to the contribution are in the same ratio as their interests in the capital and profits of the partnership after the contribution. Where these conditions are met, depreciation, depletion, or gain or loss with respect to the undivided interests in contributed property shall be determined in the same manner as though such undivided interests continued to be held by the partners outside the partnership. The rule stated in section 704 (c) (3) applies both to the case where persons knowingly contribute undivided interests to a partnership and to the case where owners of undivided interests in property, by virtue of the joint conduct of business activity, are determined to be a partnership under subchapter K. This provision may be illustrated by the following examples:

Example (1). A and B are tenants in common owning undivided one-half interests in improved real estate consisting of land on which a factory is situated. They each contribute their respective undivided interests in the real estate to a partnership in which the profits are to be divided equally and the assets are to be divided equally on dissolution. A's basis for his undivided one-half interest is $4,000, of which $1,000 is allocable to the land and $3,000 to the factory. B's basis for his undivided one-half interest is $10,000, of which $3,000 is allocable to the land and $7,000 to the factory. The partnership agreement contains no provisions as to the allocation of depreciation or gain or loss on disposition of the property by the partnership. The factory depreciates at a rate of 5 percent a year. The annual partnership allowance for depreciation of $500 (5 percent of $10,000) will be allocated between the partners by allowing A a deduction of $150 (5 percent of $3,000, his basis for his undivided interest in the factory) and by allowing B a deduction of $350 (5 percent of $7,000, his basis for his undivided interest in the factory). At the end of the first year of partnership operation, A's adjusted basis for his undivided interest in the factory would be $2,850 ($3,000 less $150), and B's adjusted basis would be $6,650 ($7,000 less $350).

Example (2). If, in the above example, the partnership at the end of the first year's operation sells the factory and land for $20,000, each partner's share of the gain would be determined as follows: Since the undivided interests in the factory and the land are to be treated as though held by the partners outside the partnership, A's share of the proceeds of the sale is $10,000. His adjusted basis in the contributed property is $3,850 ($1,000 for the land and $2,850 for the factory). Therefore, his gain from the sale is $6,150. Since B's share is also $10,000, and his adjusted basis in the contributed property is $9,650 ($3,000 for the land $6,650 for the factory), his gain is $350.

(ii) The allocation illustrated in subdivision (i) of this subparagraph will not be affected by the contribution, either at

the time of the original contribution or subsequent thereto, of additional property not held in the form of undivided interests if the partners' respective interests in the capital and profits of the partnership remain the same as their undivided interests in the property previously contributed to the partnership. If the partners' interests are changed as the result of a further contribution of property and by a modification of the partnership agreement, the method of allocation of depreciation, depletion, or gain or loss with respect to the property formerly held in the form of undivided interests would no longer apply. However, the partners may agree under section 704 (c) (2) at the time of the additional contribution of property that depreciation, depletion, or gain or loss with respect to the property shall continue to be allocated as if such property had not been contributed to the partnership. These provisions may be illustrated by the following examples:

Example (1). C and D are tenants in common, each owning an undivided one-half interest in certain unimproved land. Each contributes his respective undivided interest in the land to a partnership in which each has an equal interest. C's basis for his one-half interest is $4,000; D's basis is $10,000. The fair market value of the land is $20,000. Subsequently, C makes a further contribution of $5,000 in cash. The partners agree that in consideration of C's additional contribution he is to have a 60-percent interest in partnership capital and profits and D a 40-percent interest. Since the interests of the partners in the capital and profits of the partnership no longer correspond to their undivided interests in the land, the method of allocation prescribed by section 704 (c) (3) no longer applies. Therefore, if the land is sold for $25,000, the partnership will have a gain of $11,000 ($25,000 minus $14,000 parnership basis). 60 percent of this gain is allocated to C and 40 percent to D.

Example (2). Assume in the above example that the partners agree at the time of C's additional contribution of $5,000 that he is to have a 60-percent interest in partnership capital and profits but that, under section 704 (c) (2), depreciation, depletion, or gain or loss with respect to the land is to continue to be allocated in the same manner as these items would have been allocated prior to contribution. The land is sold for $25,000. C's share of the proceeds is $12,500. His basis for the land is $4,000. Therefore, he has a $8,500 gain. D's gain is $2,500 ($12,500 proceeds less $10,000 basis).

(d) *Limitation on allowance of losses.* A partner's distributive share of partnership loss (including capital loss) will be allowed only to the extent of the adjusted basis of such partner's interest in the partnership at the end of the partnership taxable year in which such loss occurred. An excess of the partner's share of such loss over his adjusted basis at the end of the partnership taxable year will not be allowed for that year. However, any loss previously disallowed will be allowed at the end of a subsequent partnership taxable year to the extent of the partner's adjusted basis for his partnership interest at the end of that year. For the determination of basis of a partner's interest and the treatment of certain liabilities of the partner or partnership, see sections 705 and 752 and §§ 1.705–1 and 1.752–1. The provisions of this paragraph may be illustrated by the following examples:

Example (1). At the end of the partnership taxable year 1955, partnership AB has a loss of $20,000. Partner A's distributive share of this loss is $10,000. At the end of such year, A's adjusted basis for his interest in the partnership (not taking into account his distributive share of the loss) is $6,000. Under section 704 (d), A's distributive share of partnership loss is allowed to him (in his taxable year within or with which the partnership taxable year ends) only to the extent of his adjusted basis of $6,000. The $6,000 loss allowed decreases the adjusted basis of his interest to zero. Assume that at the end of partnership taxable year 1956, the adjusted basis of A's interest in the partnership has increased to $3,000 (not taking into account the $4,000 loss disallowed in 1955). $3,000 of the $4,000 loss disallowed for the partnership taxable year 1955 is allowed A for the partnership taxable year 1956, thus again decreasing the adjusted basis of his interest to zero. If at the end of partnership taxable year 1957, A has an adjusted basis of his interest of at least $1,000 (not taking into account the disallowed loss of $1,000), he will be allowed the $1,000 loss previously disallowed.

Example (2). At the end of partnership taxable year 1955, partnership CD has a loss of $20,000. Partner C's distributive share of this loss is $10,000. The adjusted basis of his interest in the partnership (not taking into account his distributive share of such loss) is $6,000. Therefore, $4,000 of the loss is disallowed him. In partnership taxable year 1956, the partnership has no taxable income or loss but borrows $8,000 from a bank. Since C's proportionate share of this liability is $4,000, the basis of his partnership interest is increased from zero to $4,000. (See sections 752 and 722.) C is allowed the $4,000 loss (previously disallowed under section 704 (d)) for his taxable year within or with which partnership taxable year 1956 ends.

(e) *Family partnerships*—(1) *In general*—(i) *Introduction.* The production of income by a partnership is attributable to the capital or services, or both, contributed by the partners. The provisions of subchapter K are to be read in the light of their relationship to section 61, which requires that income be taxed to the person who earns it through his own labor and skill and the utilization of his own capital.

(ii) *Recognition of donee as partner* With respect to partnerships in which capital is a material income-producing factor, section 704 (e) (1) provides that a person shall be recognized as a partner for income tax purposes if he owns a capital interest in such a partnership, whether or not such interest is derived by purchase or gift from any other person. If a capital interest in a partnership in which capital is a material income-producing factor is created by gift, section 704 (e) (2) provides that the distributive share of the donee under the partnership agreement shall be includible in his gross income, except to the extent that such distributive share is determined without allowance of reasonable compensation for services rendered to the partnership by the donor, and except to the extent that the portion of such distributive share attributable to donated capital is proportionately greater than the share of the donor attributable to the donor's capital. For rules of allocation in such cases, see subparagraph (3)

(iii) *Requirement of complete transfer to donee.* A donee or purchaser of a capital interest in a partnership is not recognized as a partner under the principles of section 704 (e) (1) unless such interest is acquired in a bona fide transaction, not a mere sham for tax avoidance or evasion purposes, and the donee or purchaser is the real owner of such interest. To be recognized, a transfer must vest dominion and control of the partnership interest in the transferee. The existence of such dominion and control in the donee is to be determined from all the facts and circumstances. A transfer is not recognized if the transferor retains such incidents of ownership that the transferee has not acquired full and complete ownership of the partnership interest. Transactions between members of a family will be closely scrutinized, and the circumstances not only at the time of the purported transfer but also during the periods preceding and following it will be taken into consideration in determining the bona fides or lack of bona fides of the purported gift or sale. A partnership may be recognized for income tax purposes as to some partners but not as to others.

(iv) *Capital as a material income-producing factor.* For purposes of section 704 (e) (1), the determination as to whether capital is a material income-producing factor must be made by reference to all the facts of each case. Capital is a material income-producing factor if a substantial portion of the gross income of the business is attributable to the employment of capital in the business conducted by the partnership. In general, capital is not a material income-producing factor where the income of the business consists principally of fees, commissions, or other compensation for personal services performed by members or employees of the partnership. On the other hand, capital is ordinarily a material income-producing factor if the operation of the business requires substantial inventories or a substantial investment in plant, machinery, or other equipment.

(v) *Capital interest in a partnership.* For purposes of section 704 (e) a capital interest in a partnership means an interest in the capital of the partnership, including additions thereto, which interest is distributable to the owner of the capital interest upon his withdrawal from the partnership or upon liquidation of the partnership. The mere right to participate in the earnings and profits of a partnership is not a capital interest in the partnership.

(2) *Basic tests as to ownership*—(i) *In general.* Whether an alleged partner who is a donee of a capital interest in a partnership is the real owner of such capital interest, and whether the donee has dominion and control over such interest, must be ascertained from all the facts and circumstances of the particular case. Isolated facts should not be considered determinative; the reality of the donee's ownership is to be determined in the light of the transaction as a whole.

The execution of legally sufficient and irrevocable deeds or other instruments of gift under State law is a factor to be taken into account but is not determinative of ownership by the donee for the purposes of section 704 (e) The reality of the transfer and of the donee's ownership of the property attributed to him are to be ascertained from the conduct of the parties with respect to the alleged gift and not by any mechanical or formal test. Some of the more important factors to be considered in determining whether the donee has acquired ownership of the capital interest in a partnership are indicated in subdivisions (ii) to (x) inclusive, of this subparagraph.

(ii) *Retained controls.* The donor may have retained such controls of the interest which he has purported to transfer to the donee that the donor should be treated as remaining the substantial owner of the interest. Controls of particular significance include, for example, the following:

(*a*) Retention of control of the distribution of amounts of income or restrictions on the distributions of amounts of income (other than amounts retained in the partnership annually with the consent of the partners, including the donee partner, for the reasonable needs of the business) If there is a partnership agreement providing for a managing partner or partners, then amounts of income may be retained in the partnership without the acquiescence of all the partners if such amounts are retained for the reasonable needs of the business.

(*b*) Limitation of the right of the donee to liquidate or sell his interest in the partnership at his discretion without financial detriment.

(*c*) Retention of control of assets essential to the business (for example, through retention of assets leased to the alleged partnership)

(*d*) Retention of management powers inconsistent with normal relationships among partners. Retention by the donor of control of business management or of voting control, such as is common in ordinary business relationships, is not by itself to be considered as inconsistent with normal relationships among partners, provided the donee is free to liquidate his interest at his discretion without financial detriment. The donee shall not be considered free to liquidate his interest unless, considering all the facts, it is evident that the donee is independent of the donor and has such maturity and understanding of his rights as to be capable of deciding to exercise, and capable of exercising, his right to withdraw his capital interest from the partnership.

The existence of some of the indicated controls, though amounting to less than substantial ownership retained by the donor, may be considered along with other facts and circumstances as tending to show the lack of reality of the partnership interest of the donee.

(iii) *Indirect controls.* Controls inconsistent with ownership by the donee may be exercised indirectly as well as directly, for example, through a separate business organization, estate, trust, individual, or other partnership. Where such indirect controls exist, the reality of the donee's interest will be determined as if such controls were exercisable directly.

(iv) *Participation in management.* Substantial participation by the donee in the control and management of the business (including participation in the major policy decisions affecting the business) is strong evidence of a donee partner's exercise of dominion and control over his interest. Such participation presupposes sufficient maturity and experience on the part of the donee to deal with the business problems of the partnership.

(v) *Income distributions.* The actual distribution to a donee partner of the entire amount or a major portion of his distributive share of the business income for the sole benefit and use of the donee is substantial evidence of the reality of the donee's interest, provided the donor has not retained controls inconsistent with real ownership in the donee. Amounts distributed are not considered to be used for the donee's sole benefit if, for example, they are deposited, loaned, or invested in such manner that the donor controls or can control the use or enjoyment of such funds.

(vi) *Conduct of partnership business.* In determining the reality of the donee's ownership of a capital interest in a partnership, consideration shall be given to whether the donee is actually treated as a partner in the operation of the business. Whether or not the donee has been held out publicly as a partner in the conduct of the business, in relations with customers, or with creditors or other sources of financing, is of primary significance. Other factors of significance in this connection include:

(*a*) Compliance with local partnership, fictitious names, and business registration statutes.

(*b*) Control of business bank accounts.

(*c*) Recognition of the donee's rights in distributions of partnership property and profits.

(*d*) Recognition of the donee's interest in insurance policies, leases, and other business contracts and in litigation affecting business.

(*e*) The existence of written agreements, records, or memoranda, contemporaneous with the taxable year or years concerned, establishing the nature of the partnership agreement and the rights and liabilities of the respective partners.

(*f*) Filing of partnership tax returns as required by law.

However, despite formal compliance with the above factors, other circumstances may indicate that the donor has retained substantial ownership of the interest purportedly transferred to the donee.

(vii) *Trustees as partners.* A trustee may be recognized as a partner for income tax purposes under the principles relating to family parnerships generally as applied to the particular facts of the trust-partnership arrangement. A trustee who is unrelated to and independent of the grantor, and who participates as a partner and receives distribution of the income distributable to the trust, will ordinarily be recognized as the owner of the partnership interest which he holds for the trust unless the grantor has retained controls inconsistent with such ownership. However, if the grantor is the trustee, or if the trustee is amenable to the will of the grantor, the provisions of the trust instrument (particularly as to whether the trustee is subject to the responsibilities of a fiduciary), the provisions of the partnership agreement, and the conduct of the parties must all be taken into account in determining whether the trustee in a fiduciary capacity has become the real owner of the partnership interest. Where the grantor (or person amenable to his will) is the trustee, the trust may be recognized as a partner only if the grantor (or such other person) in his participation in the affairs of the partnership actively represents and protects the interests of the beneficiaries in accordance with the obligations of a fiduciary and does not subordinate such interests to the interests of the grantor. Furthermore, if the grantor (or person amenable to his will) is the trustee, the following factors will be given particular consideration:

(*a*) Whether the trust is recognized as a partner in business dealings with customers and creditors, and

(*b*) Whether, if any amount of the partnership income is not properly retained for the reasonable needs of the business, the trust's share of such amount is distributed to the trust annually and paid to the beneficiaries or reinvested solely in the interests of the beneficiaries.

(viii) *Interests (not held in trust) of minor children.* Except where a minor child is shown to be competent to manage his own property and participate in the partnership activities in accordance with his interest in the property, a minor child generally will not be recognized as a member of a partnership unless control of the property and its enjoyment is exercised by another person as fiduciary for the sole benefit of the child, and unless there is such judicial supervision of the conduct of the fiduciary as is required by law. The use of the child's property or income for support for which a parent is legally responsible will be considered a use for the parent's benefit. "Judicial supervision of the conduct of the fiduciary" includes filing of such accountings and reports as are required by law of the fiduciary who participates in the affairs of the partnership on behalf of the minor. A minor child will be considered as competent to manage his own property if he actually has sufficient maturity and experience to be treated by disinterested persons as competent to enter business dealings and otherwise to conduct his affairs on a basis of equality with adult persons, notwithstanding legal disabilities of the minor under State law.

(ix) *Donees as limited partners.* The recognition of a donee's interest in a limited partnership will depend, as in the case of other donated interests, on whether the transfer of property is real and on whether the donee has acquired dominion and control over the interest purportedly transferred to him. To be recognized for Federal income tax pur-

poses, a limited partnership must be organized and conducted in accordance with the requirements of the applicable State limited-partnership law. The absence of services and participation in management by a donee in a limited partnership is immaterial if the limited partnership meets all the other requirements prescribed in paragraph (e) If the limited partner's right to transfer or liquidate his interest is subject to substantial restrictions (for example, where the interest of the limited partner is not assignable in a real sense or where such interest may be required to be left in the business for a long term of years) or if the general partner retains any other control which substantially limits any of the rights which would ordinarily be exercisable by unrelated limited partners in normal business relationships, such restrictions on the right to transfer or liquidate, or retention of other control, will be considered strong evidence as to the lack of reality of ownership by the donee.

(x) *Motive.* If the reality of the transfer of interest is satisfactorily established, the motives for the transaction are generally immaterial. However, the presence or absence of a tax-avoidance motive is one of many factors to be considered in determining the reality of the ownership of a capital interest acquired by gift.

(3) *Allocation of family partnership income*—(i) *In general.* (*a*) Where a capital interest in a partnership in which capital is a material income-producing factor is created by gift, the donee's distributive share shall be includible in his gross income, except to the extent that such share is determined without allowance of reasonable compensation for services rendered to the partnership by the donor, and except to the extent that the portion of such distributive share attributable to donated capital is proportionately greater than the distributive share attributable to the donor's capital. For the purpose of this section, a capital interest in a partnership purchased by one member of a family from another shall be considered to be created by gift from the seller, and the fair market value of the purchased interest shall be considered to be donated capital. The "family" of any individual, for the purpose of the preceding sentence, shall include only his spouse, ancestors, and lineal descendants, and any trust for the primary benefit of such persons.

(*b*) To the extent that the partnership agreement does not allocate the partnership income in accordance with subdivision (*a*) above, the distributive shares of the partnership income of the donor and donee shall be reallocated by making a reasonable allowance for the services of the donor and by attributing the balance of such income (other than a reasonable allowance for the services, if any, rendered by the donee) to the partnership capital of the donor and donee. The portion of income, if any, thus attributable to partnership capital for the taxable year shall be allocated between the donor and donee in accordance with their respective interests in partnership capital.

(*c*) In determining a reasonable allowance for services rendered by the partners, consideration shall be given to all facts and circumstances of the business, including the fact that some of the partners may have greater managerial responsibility than others. There shall also be considered the amount that would ordinarily be paid in order to obtain comparable services from a person not having a capital interest in the partnership.

(*d*) The distributive share of partnership income, as determined under subdivision (*b*) of a partner who rendered services to the partnership before entering the Armed Forces of the United States shall not be diminished because of absence due to military service. Such distributive share shall be adjusted to reflect increases or decreases in the capital interest of the absent partner. However, the partners may by agreement allocate a smaller share to the absent partner due to his absence.

(ii) *Special rules.* (*a*) The provisions of subdivision (i) of this subparagraph (relating to allocation of family partnership income) are applicable where the interest in the partnership is created by gift, indirectly or directly. Where the partnership interest is created indirectly, the term "donor" may include persons other than the nominal transferor. This rule may be illustrated by the following examples:

Example (*1*). A father gives property to his son who shortly thereafter conveys the property to a partnership consisting of the father and the son. The partnership interest of the son may be considered created by gift and the father may be considered the donor of the son's partnership interest.

Example (*2*). A father, the owner of a business conducted as a sole proprietorship, transfers the business to a partnership consisting of his wife and himself. The wife subsequently conveys her interest to their son. In such case, the father, as well as the mother, may be considered the donor of the son's partnership interest.

Example (*3*). A father makes a gift to his son of stock in the family corporation. The corporation is subsequently liquidated. The son later contributes the property received in the liquidation of the corporation to a partnership consisting of his father and himself. In such case, the son's partnership interest may be considered created by gift and the father may be considered the donor of his son's partnership interest.

(*b*) The allocation rules set forth in section 704 (e) and subdivision (i) of this subparagraph apply in any case in which the transfer or creation of the partnership interest has any of the substantial characteristics of a gift. Thus, allocation may be required where transfer of a partnership interest is made between members of a family (including collaterals) under a purported purchase agreement, if the characteristics of a gift are ascertained from the terms of the purchase agreement, the terms of any loan or credit arrangements made to finance the purchase, or from other relevant data.

(*c*) In the case of a limited partnership, for the purpose of the allocation provisions of subdivision (i) of this subparagraph, consideration shall be given to the fact that a general partner, unlike a limited partner, risks his credit in the partnership business.

(4) *Purchased interest*—(i) *In general.* If a purported purchase of a capital interest in a partnership does not meet the requirements of subdivision (ii) of this subparagraph, the ownership by the transferee of such capital interest will be recognized only if it qualifies under the requirements applicable to a transfer of a partnership interest by gift. In a case not qualifying under subdivision (ii), if payment of any part of the purchase price is made out of partnership earnings, the transaction may be regarded in the same light as a purported gift subject to deferred enjoyment of income. Such a transaction may be lacking in reality either as a gift or as a bona fide purchase.

(ii) *Tests as to reality of purchased interests.* A purchase of a capital interest in a partnership, either directly or by means of a loan or credit extended by a member of the family, will be recognized as bona fide under either of the following tests:

(*a*) If it can be shown that the purchase has the usual characteristics of an arm's-length transaction, considering all relevant factors, including the terms of the purchase agreement (as to price, due date of payment, rate of interest, and security, if any) and the terms of any loan or credit arrangement collateral to the purchase agreement; the credit standing of the purchaser, apart from relationship to the seller; and the capacity of the purchaser to incur a legally binding obligation; or

(*b*) If it can be shown, in the absence of characteristics of an arm's-length transaction, that the purchase was genuinely intended to promote the success of the business by securing participation of the purchaser in the business or by adding his credit to that of the other participants. However, if the alleged purchase price or loan has not been paid or the obligation otherwise discharged, the factors indicated in subdivision (*a*) and this subdivision shall be taken into account only as an aid in determining whether a bona fide purchase or loan obligation existed.

§ 1.705 *Statutory provisions; determination of basis of partner's interest.*

SEC. 705. *Determination of basis of partner's interest*—(a) *General rule.* The adjusted basis of a partner's interest in a partnership shall, except as provided in subsection (b), be the basis of such interest determined under section 722 (relating to contributions to a partnership) or section 742 (relating to transfers of partnership interests)—

(1) Increased by the sum of his distributive share for the taxable year and prior taxable years of—

(A) Taxable income of the partnership as determined under section 703 (a),

(B) Income of the partnership exempt from tax under this title, and

(C) The excess of the deductions for depletion over the basis of the property subject to depletion; and

(2) Decreased (but not below zero) by distributions by the partnership as provided in section 733 and by the sum of his distributive share for the taxable year and prior taxable years of—

(A) Losses of the partnership, and

(B) Expenditures of the partnership not deductible in computing its taxable income and not properly chargeable to capital account.

(b) *Alternative rule.* The Secretary or his delegate shall prescribe by regulations the circumstances under which the adjusted basis of a partner's interest in a partnership may be determined by reference to his proportionate share of the adjusted basis of partnership property upon a termination of the partnership.

§ 1.705–1 *Determination of basis of partner's interest*—(a) *General rule.* (1) Section 705 and this section provide rules for determining the adjusted basis of a partner's interest in a partnership. A partner is required to determine the adjusted basis of his interest in a partnership only when necessary for the determination of his tax liability or that of any other person. The determination of the adjusted basis of a partnership interest is ordinarily made as of the end of a partnership taxable year. However, where there has been a sale or exchange of a partnership interest or a liquidation of a partner's entire interest in a partnership, the adjusted basis of the partner's interest should be determined as of the date of sale or exchange or liquidation. The adjusted basis of a partner's interest in a partnership is determined without regard to any amount shown in the partnership books as the partner's "capital" or "equity" account, etc. For example, A contributes property with an adjusted basis to him of $400 (and a value of $1,000) to a partnership. B contributes $1,000 cash. While under their agreement each may have a "capital" account in the partnership of $1,000, the adjusted basis of A's interest is $400 and B's interest $1,000.

(2) The original basis of a partner's interest in a partnership shall be determined under section 722 (relating to contributions to a partnership) or section 742 (relating to transfers of partnership interests) The basis so determined shall be increased by any further contributions to the partnership in accordance with section 722 and by the sum of the partner's distributive share for the taxable year and prior taxable years of—

(i) Taxable income of the partnership as determined under section 703 (a)

(ii) Tax-exempt receipts of the partnership, and

(iii) The excess of the deduction for depletion over the basis of depletable property.

(3) The basis shall be decreased (but not below zero) by distributions from the partnership as provided in section 733 and by the sum of the partner's distributive share for the taxable year and prior taxable years of—

(i) Partnership losses (including capital losses) and

(ii) Partnership expenditures which are not deductible in computing taxable income and which are not capital expenditures.

(4) In determining the amount of contributions made by a partner to a partnership or the amount of distributions made by a partnership to a partner, see section 752 and § 1.752–1, relating to the treatment of certain liabilities.

(b) *Alternative rule.* In certain cases, the adjusted basis of a partner's interest in a partnership may be determined by reference to the partner's proportionate share of the adjusted basis of partnership property which would be distributable upon termination of the partnership. The alternative rule may be used to determine the adjusted basis of a partner's interest where circumstances are such that the partner cannot apply the general rule set forth in section 705 (a) and paragraph (a) and where, from a consideration of all the facts, it is, in the opinion of the Commissioner, reasonable to conclude that the result produced will not vary substantially from the result obtainable under the general rule. In certain cases, adjustments may be necessary in determining the adjusted basis of a partner's interest in a partnership under the alternative rule. Adjustments would be required, for example, in order to reflect in a partner's proportionate share of the adjusted basis of partnership property any significant discrepancies arising as a result of contributed property, transfers of partnership interests, or distributions of property to the partners. The operation of the alternative rule may be illustrated by the following examples:

Example (1). The AB partnership, in which A and B are equal partners, owns property with an adjusted basis of $1,000 and has earned and retained an additional $1,000. The total adjusted basis of partnership property is $2,000. The proportionate share of each partner in the adjusted basis of partnership property is one-half of this amount, or $1,000. Under the alternative rule, this amount represents each partner's adjusted basis for his partnership interest. If $250 is distributed to each partner, his basis becomes $750, or one-half of the remaining $1,500 partnership basis. If $350 had been distributed to A and $150 to B, A's basis would be $650 ($1,000 minus $350) · B's basis would be $850 ($1,000 minus $150).

Example (2). Assume that partner A in example (1) sells his partnership interest to C for $1,250 at a time when the partnership property with an adjusted basis of $1,000 had appreciated in value to $2,000, and when the partnership also has $500 in cash. The adjusted basis of partnership property is $1,500 and the value of such property is $2,500. C's basis for his partnership interest is his cost, $1,250. However, his one-half share of the adjusted basis of partnership property is only $750. Therefore, for the purposes of the alternative rule, C has an adjustment of $500 in determining the basis of his interest. This amount represents the difference between the cost of his partnership interest and his pro rata share of partnership basis at the time of purchase. If the partnership now earns and retains an additional $1,000, its property will have an adjusted basis of $2,500 and a value of $3,500. C's adjusted basis for his interest under the alternative rule is $1,750, determined by adding $500, his basis adjustment, to $1,250 (his one-half share of the $2,500 adjusted basis of partnership property). If the partnership currently distributes $250 to each partner, C's adjusted basis for his interest would be $1,500 ($1,000, his one-half share of the remaining basis of partnership property, $2,000, plus his basis adjustment of $500).

Example (3). Assume that BC partnership in example (2) continues to operate. In 1960, C proposes to sell his partnership interest and wishes to evaluate the tax consequences of such sale. It is necessary, therefore, to determine the adjusted basis of his interest in the partnership. Assume further that C cannot determine the adjusted basis of his interest under the general rule and that there is no reason to believe that the result to be obtained under the alternative rule will vary substantially from the result under the general rule. The balance sheet of the BC partnership follows:

	Adjusted basis per books	Market value
ASSETS		
Cash	$3,000	$3,000
Receivables	4,000	4,000
Depreciable property	5,000	5,000
Land held for investment	18,000	30,000
Total	30,000	42,000
LIABILITIES AND CAPITAL	Per books	
Liabilities	$6,000	.....
Capital accounts:		
B	9,000	.....
C	15,000	.....
Total	30,000	.....

The $15,000 representing the amount of C's capital account does not reflect the $500 basis adjustment arising from C's purchase of his interest. See example (2). The adjusted basis of C's partnership interest determined under the alternative rule is as follows:

C's proportionate share of the adjusted basis of partnership property (reduced by the amount of liabilities) at time of proposed sale (15,000/24,000 of $24,000)	$15,000
C's proportionate share of partnership liabilities (under the partnership agreement liabilities are shared equally)	3,000
C's basis adjustment from example (2)	500
Adjusted basis of C's interest at the time of proposed sale as determined under alternative rule	18,500

§ 1.706 *Statutory provisions; taxable years of partner and partnership.*

SEC. 706. *Taxable years of partner and partnership*—(a) *Year in which partnership income is includible.* In computing the taxable income of a partner for a taxable year, the inclusions required by section 702 and section 707 (c) with respect to a partnership shall be based on the income, gain, loss, deduction, or credit of the partnership for any taxable year of the partnership ending within or with the taxable year of the partner.

(b) *Adoption of taxable year*—(1) *Partnership's taxable year.* The taxable year of a partnership shall be determined as though the partnership were a taxpayer. A partnership may not change to, or adopt, a taxable year other than that of all its principal partners unless it establishes, to the satisfaction of the Secretary or his delegate, a business purpose therefor.

(2) *Partner's taxable year.* A partner may not change to a taxable year other than that of a partnership in which he is a principal partner unless he establishes, to the satisfaction of the Secretary or his delegate, a business purpose therefor.

(3) *Principal partner.* For the purpose of this subsection, a principal partner is a partner having an interest of 5 percent or more in partnership profits or capital.

(c) *Closing of partnership year*—(1) *General rule.* Except in the case of a termination of a partnership and except as provided in paragraph (2) of this subsection, the taxable year of a partnership shall not close as the result of the death of a partner, the entry

of a new partner, the liquidation of a partner's interest in the partnership, or the sale or exchange of a partner's interest in the partnership.

(2) *Partner who retires or sells interest in partnership*—(A) *Disposition of entire interest.* The taxable year of a partnership shall close—

(i) With respect to a partner who sells or exchanges his entire interest in a partnership, and

(ii) With respect to a partner whose interest is liquidated, except that the taxable year of a partnership with respect to a partner who dies shall not close prior to the end of the partnership's taxable year.

Such partner's distributive share of items described in section 702 (a) for such year shall be determined, under regulations prescribed by the Secretary or his delegate, for the period ending with such sale, exchange, or liquidation.

(B) *Disposition of less than entire interest.* The taxable year of a partnership shall not close (other than at the end of a partnership's taxable year as determined under subsection (b) (1)) with respect to a partner who sells or exchanges less than his entire interest in the partnership or with respect to a partner whose interest is reduced, but such partner's distributive share of items described in section 702 (a) shall be determined by taking into account his varying interests in the partnership during the taxable year.

§ 1.706–1 *Taxable years of partner and partnership*—(a) *Year in which partnership income is includible.* In computing his taxable income for a taxable year, a partner is required to include his distributive share of partnership items set forth in section 702 for any partnership year ending within or with his taxable year. A partner shall also include in his taxable income for a taxable year "guaranteed payments" under section 707 (c) which are made to him in a partnership taxable year ending within or with his taxable year. The provisions of this paragraph may be illustrated by the following example:

Example. Partner A reports his income for a calendar year while the partnership of which he is a member reports its income for a fiscal year ending May 31. During the partnership taxable year ending May 31, 1956, A received guaranteed payments of $1,200 for services and for the use of capital. Of this amount, $700 was received by A between June 1 and December 31, 1955, and the remaining $500 was received by him between January 1 and May 31, 1956. This entire $1,200 received by A is includible in his taxable income for the calendar year 1956 (together with his distributive share of partnership items set forth in section 702 for the partnership taxable year ending May 31, 1956).

(b) *Adoption or changes of taxable year*—(1) *Partnership taxable year.* The taxable year of a partnership shall be determined as though the partnership were a taxpayer. An existing partnership may not change to a taxable year other than that which is the same as that of all of its principal partners unless it obtains prior approval from the Commissioner. A newly formed partnership which wishes to adopt a taxable year which is different from the taxable year of any of its principal partners must secure prior approval from the Commissioner, except that a new partnership may adopt a calendar year without securing prior approval if all the principal partners are not on the same taxable year. Prior approval will not be required if—

(i) All the principal partners have the same taxable year which the partnership adopts or to which it changes, or

(ii) All principal partners having a different taxable year than that which the partnership wishes to adopt or change to, concurrently change to such taxable year.

Where prior approval is required, see subparagraph (5) below.

(2) *Partner's taxable year.* A partner may not change to or adopt a taxable year which is not the same as that of every partnership in which he is a principal partner unless he obtains the prior approval of the Commissioner in accordance with subparagraph (5) below. Except as provided by section 442 and the regulations thereunder, prior approval will not be required in the case of a partner who changes to a taxable year—

(i) Which is the same as that of every partnership in which he is a principal partner, or

(ii) Which is the same as that to which every such partnership having a different taxable year concurrently changes.

(3) *Principal partner.* For the purpose of this paragraph, a principal partner is a partner having an interest of 5 percent or more in partnership profits or capital.

(4) *Returns.* (i) Any partner who changes his taxable year or any partnership which changes its taxable year shall make his or its return for a short period in accordance with section 443, except that the partnership taxable income shall not be placed on an anual basis under section 443 (b). After a change in a taxable year has been made, the income shall be computed and the returns shall be filed on the basis of the new taxable year.

(ii) Any newly formed partnership shall file with its first return a statement indicating whether the taxable year which it has adopted is the same as that of all the principal partners, or that which all of the principal partners are concurrently changing to or adopting. If all the taxable years are not the same, this statement should include the names, addresses and taxable years of the partners. If a partner or an existing partnership changes his or its taxable year, a statement setting forth the taxable years of the partners and the partnerships shall be filed with the return for the short period resulting from the change of taxable year.

(5) *Approval of change in taxable year* Where prior approval of a change in a taxable year of a partnership or a partner is required, application shall be filed in accordance with the regulations under section 442. Where prior approval is required under section 706 (b) and § 1.706–1 (b) application shall be filed with the Commissioner on or before the last day of the month following the close of the taxable year for which approval is sought. An application for a change in or adoption of a taxable year under section 706 (b) and § 1.706–1 (b) must establish a business purpose therefor to the satisfaction of the Commissioner. For example, partnership AB, which has been on a calendar year, changes its principal business activity so that its "natural business year" (the annual accounting period encompassing all related income and expense) now ends on September 30. This change may be regarded as establishing a "business purpose"

(6) *Effective date.* Section 706 (b) applies to any partnership which adopts or changes to a taxable year beginning on or after April 2, 1954. For the purpose of applying this provision, section 708 (relating to the continuation of a partnership) applies to any such taxable year. See section 771 (b) (1) and § 1.771–1 (b) (1) If a partner or a partnership has changed to or adopted as a taxable year an annual accounting period beginning on or after April 2, 1954, without obtaining prior approval of the Commissioner, and if, under the provisions of this paragraph prior approval is required for the change or adoption, such annual accounting period will not be accepted as a taxable year until approval thereof is secured. Under these circumstances, an application to change to or adopt the desired taxable year will be considered timely if filed within 90 days following the promulgation of the regulations under section 706.

(c) *Closing of partnership year*—(1) *General rule.* Section 706 (c) and this paragraph provide rules governing the closing of partnership years. The closing of a partnership taxable year or a termination of a partnership for Federal income tax purposes is not governed by the "dissolution", "liquidation" etc., of a partnership under State or local law. The taxable year of a partnership shall not close as the result of the death of a partner, the entry of a new partner, the liquidation of a partner's entire interest in the partnership (as defined in section 761 (d)), or the sale or exchange of a partner's interest in the partnership, except in the case of a termination of a partnership and except as provided in subparagraph (2) below. In the case of termination, the partnership taxable year closes for all partners as of the date of termination. See section 708 (b) and § 1.708–1 (b).

(2) *Partner who retires or sells interest in partnership*—(i) *Disposition of entire interest.* A partnership taxable year shall close with respect to (*a*) a partner who sells or exchanges his entire interest in a partnership, and (*b*) a partner whose entire interest is liquidated. However, a partnership taxable year with respect to a partner who dies shall not close prior to the end of such partnership taxable year, or the time when such partner's interest (held by his estate or other successor) is liquidated or sold or exchanged, whichever is earlier. See subparagraph (3) below.

(ii) *Inclusions in taxable income.* In the case of a sale or exchange or liquidation of a partner's entire interest, the partner shall include, in his taxable income for the taxable year within or with which his membership in the partnership ends, his distributive share of items

described in section 702 (a) for the period ending with the date of such sale, exchange, or liquidation. In order to avoid an interim closing of the partnership books, such partner's share may, by agreement among the partners, be estimated by taking the pro rata part (determined according to the portion of the taxable year of the partnership which has elapsed prior to the sale) of the amount of such items he would have included in his taxable income had he remained a partner until the end of the partnership taxable year. If this method of computing the partner's share is used, any partner who is the transferee of such partner's interest shall include in his taxable income, as his distributive share of items described in section 702 (a) with respect to the acquired interest, the pro rata part (determined according to the portion of the taxable year of the partnership which has elapsed since the acquisition of his interest) of the amount of such items he would have included had he been a partner from the beginning of the taxable year of the partnership. The application of this subdivision may be illustrated by the following example:

Example. Assume that a partner selling his partnership interest on June 30, 1955, has an adjusted basis for his interest of $5,000, that his pro rata share of partnership income up to June 30 is $15,000, and that he sells his interest for $20,000. Under the provisions of section 706 (c) (2), the partnership year with respect to him closes at the time of the sale. The $15,000 is includible in his income as his distributive share, and under section 705 it increases the basis of his partnership interest to $20,000. Therefore, no gain is recognized on the sale of his partnership interest. The purchaser of this partnership interest shall include in his income only his distributive share of partnership income for the remainder of the partnership taxable year.

(3) *Partner who dies.* When a partner dies, the partnership taxable year shall not close with respect to such partner prior to the end of the normal partnership taxable year, or prior to the time when such partner's entire interest (held by his estate or other successor) is liquidated or sold or exchanged, whichever is earlier. The partnership taxable year shall continue to its normal conclusion both for the remaining partners and with respect to the decedent partner, except that the last return of the decedent partner shall include only his share of partnership taxable income for the partnership taxable year ending within or with the last taxable year of such decedent partner (i. e., the year ending with the date of his death) The decedent's distributive share of partnership taxable income for a partnership taxable year not ending within or with the decedent's last taxable year shall be includible in the return of his estate or other successor in interest. (Such distributive share is considered income in respect of a decedent under section 691 to the extent that it is attributable to the period ending with the date of death of the decedent.) However, if under the terms of an agreement existing at the date of death of a partner, a sale or exchange of the decedent partner's entire interest in the partnership occurs upon that date, then the taxable year of the partnership with respect to such decedent partner closes upon the date of his death. (See section 706 (c) (2) (A) (i).) The sale or exchange of a partnership interest does not, for the purpose of this rule, include any transfer of a partnership interest which occurs at death as a result of inheritance or any other testamentary disposition. The provisions of this subparagraph may be illustrated by the following examples:

Example (1). B has a taxable year ending December 31 and is a member of partnership ABC, the taxable year of which ends on June 30. B dies on October 31, 1955. His estate adopts a taxable year ending December 31. The return of the decedent for the period January 1 to October 31, 1955, will include only his distributive share of taxable income of the partnership for its taxable year ending June 30, 1955. The distributive share of taxable income of the partnership for its taxable year ending June 30, 1956, attributable to the interest of the decedent, including earnings both prior to and after the decedent's death, will be includible in the return of the estate for its taxable year ending December 31, 1956. (That portion of the distributive share attributable to earnings prior to death is considered income in respect of a decedent under section 691.)

Example (2). Assume the same facts as in example (1), except that prior to B's death, B and D had agreed that upon B's death, D would purchase B's interest for $10,000. When B dies on October 31, 1955, the partnership taxable year beginning July 1, 1955, closes with respect to him. Therefore, the return for B's last taxable year (January 1 to October 31, 1955) will include his distributive share of taxable income of the partnership for its taxable year ending June 30, 1955, plus his share of partnership taxable income for the period July 1 to October 31, 1955. See § 1.706 (c) (2) (ii).

Example (3). H is a member of a partnership having a taxable year ending December 31. Both H and his son S also file calendar year returns. H dies on March 31, 1955. Administration of the estate is completed and the estate, including the partnership interest, is distributed to S as legatee on November 30, 1955. Such distribution is not considered a sale or exchange. No part of the taxable income of the partnership for the taxable year ending December 31, 1955, which is allocable to H, will be included in H's taxable income for his last taxable year (January 1 to March 31, 1955) or in the taxable income of H's estate for the taxable year April 1 to November 30, 1955. The share of partnership taxable income for the full calendar year that is allocable to H will be includible in the taxable income of S for his taxable year ending December 31, 1955.

(4) *Disposition of less than entire interest.* If a partner sells or exchanges a part of his interest in a partnership or if the interest of a partner is reduced, the partnership taxable year shall continue to its normal end. In such case, the partner's distributive share of items which he is required to include in his taxable income under the provisions of section 702 (a) shall be determined by taking into account his varying interests in the partnership during the partnership taxable year in which such sale or exchange or reduction of interest occurred.

§ 1.707 *Statutory provisions; transactions between partner and partnership.*

SEC. 707. *Transactions between partner and partnership*—(a) *Partner not acting in capacity as partner* If a partner engages in a transaction with a partnership other than in his capacity as a member of such partnership, the transaction shall, except as otherwise provided in this section, be considered as occurring between the partnership and one who is not a partner.

(b) *Certain sales or exchanges of property with respect to controlled partnerships*—(1) *Losses disallowed.* No deduction shall be allowed in respect of losses from sales or exchanges of property (other than an interest in the partnership), directly or indirectly, between—

(A) A partnership and a partner owning, directly or indirectly more than 50 percent of the capital interest, or the profits interest, in such partnership, or

(B) Two partnerships in which the same persons own, directly or indirectly, more than 50 percent of the capital interests or profits interests.

In the case of a subsequent sale or exchange by a transferee described in this paragraph, section 267 (d) shall be applicable as if the loss were disallowed under section 267 (a) (1).

(2) *Gains treated as ordinary income.* In the case of a sale or exchange, directly or indirectly, of property, which in the hands of the transferee, is property other than a capital asset as defined in section 1221—

(A) Between a partnership and a partner owning, directly or indirectly, more than 80 percent of the capital interest, or profits interest, in such partnership, or

(B) Between two partnerships in which the same persons own, directly or indirectly, more than 80 percent of the capital interests or profits interests,

any gain recognized shall be considered as gain from the sale or exchange of property other than a capital asset.

(3) *Ownership of a capital or profits interest.* For purposes of paragraphs (1) and (2) of this subsection, the ownership of a capital or profits interest in a partnership shall be determined in accordance with the rules for constructive ownership of stock provided in section 267 (c) other than paragraph (3) of such section.

(c) *Guaranteed payments.* To the extent determined without regard to the income of the partnership, payments to a partner for services or the use of capital shall be considered as made to one who is not a member of the partnership, but only for the purposes of section 61 (a) (relating to gross income) and section 162 (a) (relating to trade or business expenses).

§ 1.707–1 *Transactions between partner and partnership*—(a) *Partner not acting in capacity as partner* A partner who engages in a transaction with a partnership other than in his capacity as a partner shall be treated as if he were not a member of the partnership. Such transactions include, for example, loans by the partner to the partnership or by the partnership to the partner, the sale of property by the partner to the partnership, the purchase of property by the partner from the partnership, and the rendering of services by the partnership to the partner or by the partner to the partnership. However, transactions involving contributions of money or property by a partner to a partnership, or distributions of money or property by a partnership to a partner, are not included within the provisions of this section. In all cases the substance of the transaction will govern, rather than the form.

(b) *Certain sales or exchanges of property with respect to controlled partnerships*—(1) *Losses disallowed.* (i)

No deduction shall be allowed with respect to a loss on a sale or exchange of property (other than an interest in the partnership) directly or indirectly, between a partnership and a partner who owns, directly or indirectly, more than 50 percent of the capital interest or profits interest in such partnership. A loss on a sale or exchange of property, directly or indirectly, between two partnerships in which the same persons own, directly or indirectly, more than 50 percent of the capital interests or profits interests in each partnership shall not be allowed.

(ii) If a gain is realized upon the subsequent sale or exchange by a transferee of property with respect to which a loss was disallowed under the provisions of subdivision (i) above, section 267 (d) (relating to amount of gain where loss previously disallowed) shall apply as though the loss were disallowed under section 267 (a) (1)

(2) *Gains treated as ordinary income.* Any gain recognized upon the sale or exchange, directly or indirectly, of property which in the hands of the transferee is property other than a capital asset, as defined in section 1221, shall be ordinary income if the transaction is between a partnership and a partner who owns, directly or indirectly, more than 80 percent of the capital interest or profits interest in the partnership. This rule also applies where such a transaction is between partnerships in which the same persons own, directly or indirectly, more than 80 percent of the capital interests or profits interests in each partnership. The term "property other than a capital asset" includes (but is not limited to) depreciable property, inventory, and stock in trade.

(3) *Ownership of capital or profits interest.* For the purpose of section 707 (b) and this paragraph, the ownership of a capital interest or profits interest in a partnership shall be determined in accordance with the rules for constructive ownership of stock provided in section 267 (c) (1) (2) (4) and (5) Under these rules, ownership of a capital or profits interest in a partnership may in certain circumstances be attributed to a person who is not a partner as defined in section 761 (b)

(c) *Guaranteed payments.* For the purposes of section 61 (a) (relating to gross income) and section 162 (a) (relating to trade or business expenses) payments made by a partnership to a partner for services or for the use of capital are considered as made to a person who is not a partner, to the extent such payments are determined without regard to the income of the partnership. Accordingly, a partner must include such payments as ordinary income for his taxable year within or with which the partnership taxable year ends during which partnership taxable year such payments were deducted by the partnership as paid or accrued under its method of accounting. See section 706 (a) and § 1.706–1 (a) Guaranteed payments are not considered as made to one who is not a member of the partnership for the purposes of any provision of the internal revenue laws other than sections 61 (a) and 162 (a) For example, a partner who receives guaranteed payments for a period during which he is absent from work because of personal injuries or sickness is not entitled to exclude such payments from his gross income under section 105 (d) Similarly, a partner who receives guaranteed payments is not regarded as an employee of the partnership for the purposes of withholding of tax at source, deferred compensation plans, etc. The provisions of this paragraph may be illustrated by the following examples:

Example (1). Under the ABC partnership agreement, partner A is entitled to a fixed annual salary of $10,000 without regard to the income of the partnership. His distributive share is 10 percent. After deducting the guaranteed payment, the partnership has $50,000 ordinary income. A must include $15,000 as ordinary income for his taxable year within or with which the partnership taxable year ends ($10,000 guaranteed payment plus $5,000 distributive share).

Example (2). Partner B in the above partnership is to receive 30 percent of partnership income as determined before taking into account any guaranteed payments, but not less than $10,000. Since such income of the partnership is $60,000 ($50,000 taxable income plus $10,000 guaranteed payment to A), B received $18,000 (30 percent of $60,000) as his distributive share. No part of this amount is a guaranteed payment. However, if the partnership had $20,000 of such income (instead of $60,000), $6,000 (30 percent of $20,000) would be partner B's distributive share, and the $4,000 payable to B to bring the total amount that he is to receive to $10,000 would be a guaranteed payment.

Example (3). Partner X in the XY partnership is to receive a "salary" of $10,000 plus 30 percent of the taxable income or loss of the partnership. After deducting the salary of $10,000 paid partner X, the XY partnership has a loss of $9,000. Of this amount, $2,700 (30 percent of the loss) is X's distributive share of partnership loss and is to be taken into account by him in his return. In addition, he must report as ordinary income the guaranteed payment of $10,000 made to him by the partnership.

Example (4). Assume the same facts as in example (3) except that instead of a $9,000 loss, the partnership has $30,000 in capital gains and no other items of income or deduction, except the $10,000 paid X as a guaranteed payment. Since the items of partnership income or loss must be segregated, the partnership has a $10,000 ordinary loss and $30,000 in capital gains. X's distributive share of this amount is $3,000 ordinary loss and $9,000 capital gain. In addition, X has received a $10,000 guaranteed payment which is ordinary income to him.

§ 1.708 *Statutory provisions; continuation of partnership.*

SEC. 708. *Continuation of partnership*—(a) *General rule.* For purposes of this subchapter, an existing partnership shall be considered as continuing if it is not terminated.

(b) *Termination*—(1) *General rule.* For purposes of subsection (a), a partnership shall be considered as terminated only if—

(A) No part of any business, financial operation, or venture of the partnership continues to be carried on by any of its partners in a partnership, or

(B) Within a 12-month period there is a sale or exchange of 50 percent or more of the total interest in partnership capital and profits.

(2) *Special rules*—(A) *Merger or consolidation.* In the case of the merger or consolidation of two or more partnerships, the resulting partnership shall, for purposes of this section, be considered the continuation of any merging or consolidating partnership whose members own an interest of more than 50 percent in the capital and profits of the resulting partnership.

(B) *Division of a partnership.* In the case of a division of a partnership into two or more partnerships, the resulting partnerships (other than any resulting partnership the members of which had an interest of 50 percent or less in the capital and profits of the prior partnership) shall, for purposes of this section, be considered a continuation of the prior partnership.

§ 1.708–1 *Continuation of partnership*—(a) *General rule.* An existing partnership shall be considered as continuing if it is not terminated.

(b) *Termination*—(1) *General rule.* A partnership shall be considered as terminated only if subdivisions (i) or (ii) of this subparagraph apply.

(i) (*a*) The operations of the partnership are discontinued and no part of the partnership business, financial operation, or any venture of the partnership continues to be carried on by any of its partners in a partnership. For example, on November 20, 1956, A and B, each of whom is a 20-percent partner in partnership ABC, sell their interests to C who is a 60-percent partner. Since the business is no longer carried on by any of its partners in a partnership, the ABC partnership is considered as terminated as of November 20, 1956.

(*b*) Upon the death of one partner in a 2-member partnership, the partnership business shall not be considered as terminated if the estate or other successor in interest of the decedent partner continues as a member of the partnership.

(ii) Fifty percent or more of the total interest in partnership capital and profits is sold or exchanged within a period of 12 consecutive months. A disposition of a partnership interest by gift, bequest, or inheritance, or the liquidation of a partnership interest, is not a sale or exchange for purposes of this subparagraph. Furthermore, the contribution of property to a partnership does not constitute such a sale or exchange. Fifty percent or more of the total interest in partnership capital and profits means 50 percent or more of the total interest in partnership capital plus 50 percent or more of the total interest in partnership profits. Thus, the sale of a 30-percent interest in partnership capital and a 60-percent interest in partnership profits would not be considered the sale or exchange of 50 percent or more of the total interest in partnership capital and profits. If one or more partners sell or exchange interests aggregating 50 percent or more of the total interest in partnership capital and profits within a period of 12 consecutive months, such sale or exchange is considered as being within the provisions of this subparagraph. For example, with respect to the ABC partnership, the sale by A on May 12, 1956, of a 30-percent interest in capital and profits to D and the sale by B of a 30-percent interest in capital and profits to E on March 27, 1957, is a sale of a 50-percent or more interest. Accordingly, the partnership is considered as terminated on March 27, 1957.

(iii) For purposes of subchapter K, a partnership shall be considered as terminated and the partnership taxable year shall be considered closed as of the date on which there occurs either a cessation of operations as a partnership, as described in subdivision (i) of this subparagraph, or a sale or exchange, as described in subdivision (ii) of this subparagraph. For closing of taxable year, see section 706 (c) and § 1.706–1 (c) If a partnership is considered as terminated, the partnership properties are regarded as distributed to the partners. See sections 731 and 732 and §§ 1.731–1 and 1.732–1. See also section 751 (b) and § 1.751–1 (b) If such properties are transferred to a new partnership, they are regarded as contributions of property to that partnership.

(2) *Special rules*—(i) *Merger or consolidation.* If two or more partnerships merge or consolidate into one partnership, the resulting partnership shall be considered a continuation of that merging or consolidating partnership the members of which own an interest of more than 50 percent in the capital and profits of the resulting partnership. Any other merging or consolidating partnerships shall be considered as terminated. The taxable years of such merging or consolidating partnerships which are considered terminated shall be closed in accordance with the provisions of section 706 (c) (1) and such partnerships shall file their returns for a taxable year ending upon the date of termination, i. e., the date of merger or consolidation. The resulting partnership shall file a return for the taxable year of the merging or consolidating partnership that is considered as continuing. The return shall state that the resulting partnership is a continuation of such merging or consolidating partnership and shall include the names and addresses of the merged or consolidated partnerships. The respective distributive shares of the partners for the periods prior to and subsequent to the date of merger or consolidation shall be shown as a part of the return. The provisions of this subdivision are illustrated by the following example:

Example. Partnership AB, in whose capital and profits A and B each owns a 50-percent interest, and partnership CD, in whose capital and profits C and D each owns a 50-percent interest, merge on September 30, 1955, and form the partnership ABCD. The partners A, B, C, and D are on a calendar year; partnership AB is also on a calendar year; and partnership CD is on a fiscal year ending June 30th. After the merger, the partners have capital and profits interests as follows: A, 30 percent; B, 30 percent; C, 20 percent; and D, 20 percent. Since A and B together own an interest of more than 50 percent in the capital and profits of partnership ABCD, such partnership shall be considered a continuation of partnership AB and will continue to file returns on a calendar year basis. Since C and D own an interest in capital and profits of ABCD partnership of less than 50 percent, the taxable year of partnership CD will close as of September 30, 1955, the date of the merger, and CD partnership will be considered terminated as of that date. Partnership ABCD is required to file a return for the taxable year January 1 to December 31, 1955, indicating thereon that until September 30, 1955, it was partnership AB. Partnership CD will be required to file a return for its taxable year July 1, 1955 to September 30, 1955.

(ii) *Division of a partnership.* Upon the division of a partnership into two or more partnerships, a resulting partnership shall be considered a continuation of the prior partnership only if its members had an interest of more than 50 percent in the capital and profits of the prior partnership. Any other resulting partnership will not be considered a continuation of the prior partnership and will be considered terminated. Where members of a partnership which has been divided into two or more partnerships do not become members of a resulting partnership which is considered a continuation of the prior partnership, such partners' interests shall be considered liquidated. The resulting partnership that is regarded as continuing shall file a return for the taxable year of the partnership that has been divided. The return shall state that the partnership is a continuation of the divided partnership and shall set forth separately the respective distributive shares of the partners for the periods prior to and subsequent to the date of division. The provisions of this subdivision may be illustrated by the following example:

Example. Partnership ABCD is in the real estate and insurance business. A owns 40-percent interest, and B, C, and D each owns a 20-percent interest, in the capital and profits of the partnership. The partnership and the partners report their income on a calendar year. They agree to separate the real estate and insurance business as of November 1, 1955. A and B take over the real estate business and C and D take over the insurance business. Since members of resulting partnership AB owned more than a 50 percent interest in the capital and profits of partnership ABCD (A, 40 percent and B, 20 percent), partnership AB shall be considered a continuation of partnership ABCD. Partnership AB will be required to file a return for the taxable year January 1 to December 31, 1955, indicating thereon that until October 31, 1955, it was partnership ABCD. Partnership CD is formed by the contribution of partners C and D of the property distributed to them in liquidation of their interests in divided partnership ABCD. It will be required to file a return for the taxable year it adopts pursuant to section 706 (b) and § 1.706–1 (b).

CONTRIBUTIONS, DISTRIBUTIONS, AND TRANSFERS

Contributions to a Partnership

§ 1.721 *Statutory provisions; nonrecognition of gain or loss on contribution.*

SEC. 721. *Nonrecognition of gain or loss on contribution.* No gain or loss shall be recognized to a partnership or to any of its partners in the case of a contribution of property to the partnership in exchange for an interest in the partnership.

§ 1.721–1 *Nonrecognition of gain or loss on contribution.* (a) No gain or loss shall be recognized either to the partnership or to any of its partners upon a contribution of property to the partnership in exchange for a partnership interest. This rule applies whether the contribution is made to a partnership in the process of formation or to a partnership which is already formed and operating. Section 721 shall not apply to a transaction between a partnership and a partner not acting in his capacity as a partner since such a transaction is governed by section 707. For example, if the transfer of property by the partner to the partnership results in the receipt by the partner of money or other consideration, including a promissory obligation fixed in amount and time for payment, the transaction will be treated as a sale or exchange under section 707 rather than as a contribution under section 721. In all cases the substance of the transaction will govern, rather than its form. For the rules governing the treatment of liabilities to which contributed property is subject, see section 752 and § 1.752–1.

(b) Section 721 does not apply to the extent that an interest in partnership capital is obtained by a partner as compensation for services (or in satisfaction of obligations) and not in exchange for his contribution of property to the partnership. The value of an interest in partnership capital obtained by a partner as compensation for services constitutes ordinary income to the partner under section 61. Such amount is taxable to the partner at such time as there are no substantial restrictions or conditions on his right to withdraw or otherwise dispose of such amount, or when in fact he does obtain such amount (either through a distribution or by sale or exchange of his partnership interest), whichever event first occurs. (If the partner dies prior to such realization, such amount is income in respect of a decedent under section 691.)

§ 1.722 *Statutory provisions; basis of contributing partner's interest.*

SEC. 722. *Basis of contributing partner's interest.* The basis of an interest in a partnership acquired by a contribution of property, including money, to the partnership shall be the amount of such money and the adjusted basis of such property to the contributing partner at the time of the contribution.

§ 1.722–1 *Basis of contributing partner's interest.* The basis to a partner of a partnership interest acquired by a contribution of property, including money to the partnership shall be the amount of money contributed plus the adjusted basis at the time of contribution of any property contributed. If the acquisition of an interest in a partnership results in taxable income to a partner, such income shall constitute an addition to the basis of the partner's interest. See § 1.721–1 (b) If the contributed property is subject to indebtedness or if liabilities of the partner are assumed by the partnership, the basis of the contributing partner's interest shall be reduced by the portion of the indebtedness assumed by the other partners since the transfer of such indebtedness by the partner to the partnership is treated as a distribution of money to the partner. The assumption by the other partners of a portion of the contributor's indebtedness is treated as a contribution of money by them. See section 752 and § 1.752–1. The provisions of this section may be illustrated by the following example:

Example. A acquired a 20-percent interest in a partnership by contributing $3,000 cash and certain property. At the time of A's contribution, the property had a fair market value of $6,000, an adjusted basis to A of $4,500, and was subject to a mortgage of $1,250. Payment of the mortgage was assumed by the partnership. The basis of A's interest in the partnership is $6,500, computed as follows:

Cash contributed	$3,000
Adjusted basis to A of property contributed	4,500
	7,500
Less portion of mortgage assumed by other partners (80 percent of $1,250)	1,000
Basis of A's interest	6,500

§ 1.723 *Statutory provisions; basis of property contributed to partnership.*

SEC. 723. *Basis of property contributed to partnership.* The basis of property contributed to a partnership by a partner shall be the adjusted basis of such property to the contributing partner at the time of the contribution.

§ 1.723–1 *Basis of property contributed to partnership.* The basis to the partnership of property contributed to it by a partner is the adjusted basis of such property to the contributing partner at the time of the contribution. Since such property has the same basis in the hands of the partnership as it had in the hands of the contributing partner, the holding period of such property for the partnership includes the period during which it was held by the partner. See section 1223 (2) For elective adjustments to the basis of partnership property arising from distributions or transfers of partnership interests, see sections 732 (d) 734 (b) and 743 (b)

Distributions by a Partnership

§ 1.731 *Statutory provisions; extent of recognition of gain or loss on distribution.*

SEC. 731. *Extent of recognition of gain or loss on distribution*—(a) *Partners.* In the case of a distribution by a partnership to a partner—

(1) Gain shall not be recognized to such partner, except to the extent that any money distributed exceeds the adjusted basis of such partner's interest in the partnership immediately before the distribution, and

(2) Loss shall not be recognized to such partner, except that upon a distribution in liquidation of a partner's interest in a partnership where no property other than that described in subparagraph (A) or (B) is distributed to such partner, loss shall be recognized to the extent of the excess of the adjusted basis of such partner's interest in the partnership over the sum of—

(A) Any money distributed, and

(B) The basis to the distributee, as determined under section 732, of any unrealized receivables (as defined in section 751 (c)) and inventory (as defined in section 751 (d) (2)).

Any gain or loss recognized under this subsection shall be considered as gain or loss from the sale or exchange of the partnership interest of the distributee partner.

(b) *Partnerships.* No gain or loss shall be recognized to a partnership on a distribution to a partner of property, including money.

(c) *Exceptions.* This section shall not apply to the extent otherwise provided by section 736 (relating to payments to a retiring partner or a deceased partner's successor in interest) and section 751 (relating to unrealized receivables and inventory items).

§ 1.731–1 *Extent of recognition of gain or loss on distribution*—(a) *Recognition of gain or loss to partner*—(1) *Recognition of gain.* Where money is distributed by a partnership to a partner, no gain shall be recognized to the partner except to the extent that the amount of money distributed exceeds the adjusted basis of the partner's interest in the partnership immediately before the distribution. This rule is applicable both to current distributions and to distributions in liquidation of a partner's entire interest in a partnership. Thus, if a partner with a basis for his interest of $10,000 receives a distribution of $8,000 in cash and property with a fair market value of $3,000, no gain is recognized to him. If $11,000 in cash were distributed, gain would be recognized to the extent of $1,000. No gain shall be recognized to a distributee partner with respect to a distribution of property (other than money) until he sells or otherwise disposes of such property, except to the extent otherwise provided by section 736 (relating to payments to a retiring partner or a deceased partner's successor in interest) and section 751 (relating to unrealized receivables and inventory items) See section 731 (c) and paragraph (c) below.

(2) *Recognition of loss.* Loss will be recognized to a partner only upon liquidation of his entire interest in the partnership, and only if the property distributed to him consists solely of money, unrealized receivables (as defined in section 751 (c)) and inventory items (as defined in section 751 (d) (2)) The term "liquidation of a partner's interest", as defined in section 761 (d), is the termination of the partner's entire interest in the partnership by means of a distribution or a series of distributions. Loss shall be recognized to the distributee partner in such cases to the extent of the excess of the adjusted basis of such partner's interest in the partnership at the time of the distribution over the sum of—

(i) Any money distributed to him, and

(ii) The basis to the distributee, as determined under section 732, of any unrealized receivables and inventory items that are distributed to him.

If the partner whose interest is liquidated receives any property other than money, unrealized receivables, or inventory items, then no loss will be recognized. Application of the provisions of this subparagraph may be illustrated by the following examples:

Example (1). Partner A has a partnership interest in partnership ABC with an adjusted basis to him of $10,000. He retires from the partnership and receives, as a distribution in liquidation of his entire interest, his proportionate share of partnership property. This share is $5,000 cash and inventory with a basis to him (under section 732) of $3,000. Partner A realizes a capital loss of $2,000.

Example (2). Partner B has a partnership interest in partnership BCD with an adjusted basis to him of $10,000. He retires from the partnership and receives, as a distribution in liquidation of his entire interest, his proportionate share of partnership property. This share is $4,000 cash, real property with an adjusted basis of $2,000 and unrealized receivables having a basis to him (under section 732) of $3,000. No loss will be recognized to B on the transaction because he received real property, which is property other than money, unrealized receivables, and inventory items. As determined under section 732, the basis to B for the real property received is $3,000.

(3) *Character of gain or loss.* Gain or loss recognized under section 731 (a) on a distribution is considered gain or loss from the sale or exchange of the partnership interest of the distributee partner, that is, capital gain or loss. See, however, § 1.721–1 (b) for recognition of ordinary income where interest in partnership capital is obtained as compensation for services.

(b) *Gain or loss recognized by partnership.* A distribution of property (including money) by a partnership to a partner does not result in gain or loss to the partnership under section 731. However, gain or loss may result to the partnership from certain distributions which, under section 751 (b) may be treated as a sale or exchange of property between the distributee and the partnership.

(c) *Exceptions.* (1) Section 731 does not apply to the extent otherwise provided by—

(i) Section 736 (relating to payments to a retiring partner or to a deceased partner's successor in interest) and

(ii) Section 751 (relating to unrealized receivables and inventory items)

For example, payments under 736 (a) which are considered as a distributive share or guaranteed payment, are taxable as such under that section.

(2) The receipt by a partner from the partnership of money or property under an obligation to repay the amount of such money or the value of such property does not constitute a distribution subject to section 731 but is a loan governed by section 707 (a) To the extent that such an obligation is canceled, the obligor partner will be considered to have received a distribution of money.

§ 1.732 *Statutory provisions; basis of distributed property other than money.*

SEC. 732. *Basis of distributed property other than money*—(a) *Distributions other than in liquidation of a partner's interest*—(1) *General rule.* The basis of property (other than money) distributed by a partnership to a partner other than in liquidation of the partner's interest shall, except as provided in paragraph (2), be its adjusted basis to the partnership immediately before such distribution.

(2) *Limitation.* The basis to the distributee partner of property to which paragraph (1) is applicable shall not exceed the adjusted basis of such partner's interest in the partnership reduced by any money distributed in the same transaction.

(b) *Distributions in liquidation.* The basis of property (other than money) distributed by a partnership to a partner in liquidation of the partner's interest shall be an amount equal to the adjusted basis of such partner's interest in the partnership reduced by any money distributed in the same transaction.

(c) *Allocation of basis.* The basis of distributed properties to which subsection (a) (2) or subsection (b) is applicable shall be allocated—

(1) First to any unrealized receivables (as defined in section 751 (c)) and inventory items (as defined in section 751 (d) (2)) in an amount equal to the adjusted basis of each such property to the partnership (or if the basis to be allocated is less than the sum of the adjusted bases of such properties to the partnership, in proportion to such bases), and

(2) To the extent of any remaining basis, to any other distributed properties in proportion to their adjusted bases to the partnership.

(d) *Special partnership basis to transferee.* For purposes of subsections (a), (b), and (c), a partner who acquired all or a part of his interest by a transfer with respect to which the election provided in section 754 is not in effect, and to whom a distribution of property (other than money) is made with respect to the transferred interest within 2 years after such transfer, may elect, under regulations prescribed by the Secretary or his delegate, to treat as the adjusted partnership basis of such property the adjusted basis such property would have if the adjustment provided in section 743 (b) were in effect with respect to the partnership property. The Secretary or his delegate may by regulations require the application of this subsection in the case of a distribution to a transferee partner, whether or not made within 2 years after the transfer, if at the time of the transfer the fair market value of the partnership property (other than money) exceeded 110 percent of its adjusted basis to the partnership.

(e) *Exception.* This section shall not apply to the extent that a distribution is treated as a sale or exchange of property under section 751 (b) (relating to unrealized receivables and inventory items).

§ 1.732–1 *Basis of distributed property other than money—*(a) *Distributions other than in liquidation of a partner's interest.* The unadjusted basis of property (other than money) received by a partner in a distribution from a partnership, other than in liquidation of his entire interest, shall be its adjusted basis to the partnership immediately before such distribution. However, the basis of the property to the partner shall not exceed the adjusted basis of the partner's interest in the patrnership, reduced by the amount of any money distributed to him in the same transaction. This rule may be illustrated by the following examples:

Example (1). Partner A, with an adjusted basis of $15,000 for his partnership interest, receives in a current distribution property having an adjusted basis of $10,000 to the partnership immediately before distribution, and $2,000 cash. The basis of the property in A's hands will be $10,000. Under section 733, the basis of A's partnership interest will be reduced by the distribution to $3,000 ($15,000 less $2,000 cash, less $10,000, the basis of the distributed property to A).

Example (2). Partner R has an adjusted basis of $10,000 for his partnership interest. He receives a current distribution of $4,000 in cash and property with an adjusted basis to the partnership of $8,000. The basis of the distributed property to partner R is limited to $6,000 ($10,000, the adjusted basis of his interest, reduced by $4,000, the cash distributed).

(b) *Distributions in liquidation.* Where a partnership distributes property (other than money) in liquidation of a partner's entire interest in the partnership, the basis of such property to the partner shall be an amount equal to the adjusted basis of his interest in the partnership reduced by the amount of any money distributed to him in the same transaction. Application of this rule may be illustrated by the following example:

Example. Partner B, with a partnership interest having an adjusted basis to him of $12,000, retires from the partnership and receives cash of $2,000, and real property with an adjusted basis to the partnership of $6,000 and a fair market value of $14,000. The basis of the real property to B is $10,000 (B's basis for his partnership interest, $12,000, reduced by $2,000, the cash distributed).

(c) *Allocation of basis among properties distributed to a partner* (1) The basis, under section 732 (a) (2) or (b) and § 1.732–1 (a) or (b) of properties distributed to a partner shall be allocated first to any unrealized receivables (as defined in section 751 (c)) and inventory items (as defined in section 751 (d) (2)) included in the distribution. However, such receivables or inventory items may not take a higher basis in the hands of the partner than their adjusted basis to the partnership immediately before the distribution. Any basis not allocated to unrealized receivable or inventory items shall be allocated to any other properties distributed to the partner in the same transaction, in proportion to the bases of such other properties in the hands of the partnership before distribution. The provisions of this paragraph may be illustrated by the following example:

Example. Partner A, whose partnership interest in partnership ABC has an adjusted basis of $15,000, receives as a distribution in liquidation of his entire interest inventory items having a basis to the partnership of $6,000. In addition, he receives cash of $5,000, and two parcels of real property with adjusted bases to the partnership of $6,000 and $2,000, respectively. Basis in the amount of $10,000 ($15,000 basis, less $5,000 cash received) is allocated $6,000 to inventory items and $3,000 and $1,000 to the two parcels of real property.

(2) If the adjusted basis to the partnership of the unrealized receivables and inventory items distributed to a partner is greater than the partner's adjusted basis of his interest (reduced by the amount of money distributed to him in the same transaction) the amount of the basis to be allocated to such unrealized receivables and inventory items shall be allocated in proportion to the adjusted bases of such properties in the hands of the partnership. If the basis of the partner's interest to be allocated, upon a distribution in liquidation of his entire interest, is in excess of the adjusted basis to the partnership of the unrealized receivables and inventory items distributed, and if there is no other property distributed to which such excess can be allocated, the distributee partner sustains a capital loss under section 731 (a) (2) to the extent of the unallocated basis of his partnership interest. The provisions of this subparagraph may be illustrated by the following examples:

Example (1). Partner C, whose interest in partnership ABC has an adjusted basis to him of $9,000, receives as a distribution in liquidation cash of $6,000, inventory items having an adjusted basis to the partnership of $6,000, and real property having a basis to the partnership of $4,000. The cash payment reduces C's basis to $3,000, which is allocated entirely to inventory items. The real property has a zero basis in C's hands.

Example (2). Partner B, whose interest in partnership ABC has an adjusted basis to him of $9,000, receives as a distribution in liquidation cash of $1,000 and inventory items having a basis to the partnership of $6,000. The cash payment reduces B's basis to $8,000, which can be allocated only to the extent of $6,000 to the inventory items. The remaining $2,000 basis, not allocable to distributed property, constitutes a capital loss in that amount to partner B under section 731 (a) (2).

(d) *Special partnership basis to transferee where no adjustment under section 743 is in effect.* (1) (i) Section 732 (d) provides a special rule for the determination of the basis of property distributed to a transferee partner, that is, a partner who acquired all or part of his interest by a transfer with respect to which the election under section 754 (relating to the optional adjustment to basis of partnership property under section 743 (b)) is not in effect. Where such an election is in effect, see section 743 and §§ 1.743–1 and 1.732–2. A transfer of a partnership interest occurs upon sale or exchange or upon the death of a partner. If a transferee partner receives a distribution of property (other than money) from the partnership within 2 years after he acquired his interest or part thereof in the partnership by transfer, he may elect to treat as the adjusted partnership basis of such property the adjusted basis such property would have if the adjustment provided in section 743 (b) were in effect.

(ii) If an election under section 732 (d) and this paragraph is made upon a distribution of property to a transferee partner, the amount of the adjustment with respect to the transferee partner is not diminished by any depletion or depreciation on that portion of the basis of partnership property which arises from the special basis adjustment under section 732 (d) Depletion or depreciation on such portion is only allowed or allowable if the optional adjustment under section 743 (b) is in effect.

(iii) If property is distributed to a transferee partner who has made an election under section 732 (d), and if such property is not the same property which would have had a special basis adjustment, then such special basis adjustment shall apply to any like property received in the distribution, provided that the transferee has relinquished his interest in the property with respect to which he would have had a special basis adjustment in exchange for the property distributed. This rule applies whether the property in which the transferee has relinquished his interest is retained or disposed of by the partnership. (For shift of transferee's special basis adjustment to like property, see § 1.743–1 (b) (2) (ii).)

(iv) The application of this subparagraph is illustrated by the following example:

Example. The basis to transferee partner K of his one-half interest in partnership KS is $17,000. At the time he acquired such interest by purchase, the partnership inventory had a basis to the partnership of $6,000 and had appreciated in value to $7,000.

Thus, $3,500 of the $17,000 paid by K for his one-half interest was attributable to partnership inventory. Within 2 years after acquiring his interest, K retired from the partnership and received in liquidation of his entire interest cash of $1,500, inventory with a basis to the partnership of $3,000, property A (a capital asset) with an adjusted basis to the partnership of $2,000, and property B (a depreciable asset) with an adjusted basis to the parnership of $4,000. The value of the inventory received by K was one-half of the value of all partnership inventory and was his pro rata share of such property. In accordance with K's election under section 732 (d), the amount of his share of partnership basis which is attributable to partnership inventory is increased by $500 (one-half of the $1,000 difference between the value of such property and its basis to the partnership at the time K acquired his interest). This adjustment under section 732 (d) applies only for purposes of distributions to partner K, and not for purposes of partnership depreciation, depletion, or gain or loss on disposition. Thus, the amount to be allocated among the properties received by K in the liquidating distribution is $15,500 ($17,000, K's basis for his interest, reduced, by the amount of cash received, $1,500). This amount is allocated as follows: The basis of the inventory items received is $3,500, consisting of the $3,000 common partnership basis for such items, plus the special basis adjustment of $500 which K would have had under section 743 (b). The remaining basis of $12,000 ($15,500 minus $3,500) is to be allocated to the remaining property distributed to K in proportion to their adjusted bases to the partnership. Since the adjusted basis to the partnership of property A is $2,000, and that of property B is $4,000, the $12,000 is allocated $4,000 to A, and $8,000 to B.

(2) A transferee partner who elects a special partnership basis under section 732 (d) shall submit with his income tax return for his taxable year in which the distribution is made a schedule setting forth the following information:

(i) The adjusted basis to him of his partnership interest (or such part thereof) acquired by transfer and the date of transfer;

(ii) The adjusted basis to the partnership of the property distributed, a description of the character of the property, and the date of distribution;

(iii) The amount of the special basis adjustment to be allocated under section 732 (d) to the property distributed, and the computation showing the adjustment;

(iv) The fair market value at the time of distribution of the property distributed, and the fair market value of any property of the partnership in which the transferee partner relinquished an interest in connection with the distribution; and

(v) The fair market value of the property described in (iv) above at the time the partner acquired his interest.

(3) The district director may require application of the special basis rule contained in section 732 (d) in the case of a distribution to a transferee partner, whether or not made within 2 years after the transfer, if at the time of the acquisition by the transferee of the transferred interest the fair market value of all partnership property (other than money) exceeded 110 percent of its adjusted basis to the partnership at such time. The application of this rule may be illustrated by the following example:

Example. Partnership AB owns two parcels of land each of which has an adjusted basis to the partnership of $5,000 and is worth $55,000 and depreciable property with an adjusted basis and value of $100,000. C purchases A's partnership interest for $105,000. At the time of C's purchase, the fair market value of all partnership property (other than money) is $210,000 which exceeds 110 percent of its adjusted basis to the partnership, $110,000. Four years later, the partnership is dissolved. C receives one of the two parcels of land which has a basis to the partnership of $5,000, and one-half of the depreciable property with an adjusted basis to the partnership at that time of $45,000 (one-half of $90,000, i. e., $100,000 basis minus $10,000 depreciation). If C's adjusted basis for his interest at the time of distribution, $100,000 ($105,000 minus $5,000), were allocated under section 732 (c) to the property received by him in proportion to their respective bases to the partnership, the basis to him for the distributed land would be $10,000 (5,000/50,000 x $100,000) and the basis of the depreciable property would be $90,000 (45,000/50,000 x $100,000). In effect, C would be attributing to the basis of the depreciable property a portion of the cost of his partnership interest properly attributable to appreciation in nondepreciable property. In this situation, application of the rule contained in section 732 (d) will be required by the district director so that C must increase the basis of the land by a special basis adjustment of $50,000, making the basis of his interest therein $55,000. The depreciable property will then take its carryover basis of $45,000.

(e) *Exception.* Where a partner in a distribution receives unrealized receivables (as defined in section 751 (c)) or substantially appreciated inventory items (as defined in section 751 (d)) in exchange for all or a part of his interest in other partnership property (including money) or, conversely, where a partner receives in a distribution partnership property (including money) other than unrealized receivables or substantially appreciated inventory items in exchange for all or a part of his interest in the partnership's unrealized receivables or substantially appreciated inventory items, the distribution will be treated as a sale or exchange of property under the provisions of section 751 (b) The provisions of section 732 do not apply to the extent that section 751 (b) affects any distribution of partnership property.

§ 1.732-2 *Basis of distributed property subject to adjustment.* (a) The transfer of a partnership interest in a partnership which has made an election under section 754 (relating to the optional adjustment to basis of partnership property) may result in an increase or decrease in the basis of partnership property with respect to a transferee partner. See section 743 (b) and § 1.743-1 (b) A similar adjustment may be made in certain circumstances under section 732 (d) and § 1.732-1 (d). When property is distributed by the partnership to a transferee partner, the adjusted basis to the partnership of such property immediately before its distribution shall, for the purposes of section 732, take into account any special basis adjustment under section 743 (b) or section 732 (d) that may exist for such property with respect to the transferee partner. The application of this paragraph may be illustrated by the following example:

Example. Partner C acquired his interest in partnership AC from a previous partner. Since the partnership had made an election under section 754, a special basis adjustment with respect to C is applicable to the basis of partnership property in accordance with section 743 (b). One of the assets of the partnership at the time C acquired his interest was property X, which has an adjusted basis to the partnership of $1,000 and with respect to which C has a special basis adjustment of $500. Property X is distributed to C in a current distribution. For purposes of section 732 (a) (1), the adjusted basis of such property to the partnership with respect to C immediately before its distribution is $1,500. However, if property X is distributed to partner A, a nontransferee partner, its adjusted basis to the partnership for purposes of section 732 (a) (1) is only $1,000.

(b) Under section 732 (c) (1) the basis of distributed properties to which section 732 (a) (2) or (b) is applicable shall be allocated first to any unrealized receivables and inventory items in an amount equal to the adjusted basis of such property to the partnership. See § 1.732-1 (c) If the distributee partner is a transferee of a partnership interest and has a special basis adjustment for unrealized receivables or inventory items under section 743 (b) or section 732 (d), then the partnership adjusted basis immediately prior to distribution of any unrealized receivables or inventory items distributed to such partner shall be determined as follows: If the distributee partner receives his pro rata share or more of the fair market value of the inventory items or unrealized receivables of the partnership, the adjusted basis of such distributed property to the partnership, for the purposes of section 732 (c) (1), shall be the adjusted basis of such property to the partnership plus the full amount of any special basis adjustment which the distributee partner has for such assets under section 743 (b) or section 732 (d) If the distributee partner receives less than his pro rata share of the fair market value of partnership inventory items or unrealized receivables, then for purposes of section 732 (c) (1) the adjusted basis of such distributed property to the partnership (without regard to any special basis adjustment of the distributee partner) shall be adjusted by an amount which bears the same ratio to the distributee's entire special basis adjustment for unrealized receivables or inventory items as the value of such items distributed to him bears to his pro rata share of the total value of all such items of the partnership. The provisions of this paragraph may be illustrated by the following example:

Example. Partner C acquired his half-interest in partnership AC from a previous partner. Since the partnership had made an election under section 754, C has a special basis adjustment to partnership property under section 743 (b). C retires from the partnership when the adjusted basis of his partnership interest is $3,000. He receives from the partnership in liquidation of his entire interest $1,000 cash, certain capital assets, depreciable property, and certain inventory items and unrealized receivables. C has a special basis adjustment of $800 with respect to partnership inventory items and of $200 with respect to unrealized receivables. The common partnership basis for the inventory items distributed to him is $500 and for the unrealized receivables is zero. If the value of inventory items and the unrealized receivables distributed to C is his pro rata share or more (50 percent or more) of the total value of all partnership inventory items and unrealized receivables, then for purposes of section 732 (c) (1) the ad-

justed basis of such property in C's hands will be $1,300 for the inventory items ($800 plus $500) and $200 for the unrealized receivables (zero plus $200). The remaining basis of $500, which constitutes the basis of the capital assets and depreciable property distributed to C, is determined as follows: $3,000 less $1,000 cash, or $2,000 (the amount to be allocated to the basis of all distributed property) less $1,500 ($1,000 plus $500 special basis adjustment) (the amount allocated to inventory items and unrealized receivables). However, if the value of the inventory items and unrealized receivables distributed to C consisted of only one-fourth of the total fair market value of such property (i. e., only one-half of C's pro rata share), then only one-half of C's special basis adjustment of $800 for partnership inventory items and $200 for unrealized receivables will be taken into account. Thus, the basis of the inventory items in C's hands would be $650 ($250, the common partnership basis for inventory items distributed to him, plus $400, one-half of C's special basis adjustment for inventory items). The basis of the unrealized receivables in C's hands would be $100 (zero plus $100, one-half of C's special basis adjustment for unrealized receivables).

§ 1.733 *Statutory provisions; basis of distributee partner's interest.*

SEC. 733. *Basis of distributee partner's interest.* In the case of a distribution by a partnership to a partner other than in liquidation of a partner's interest, the adjusted basis to such partner of his interest in the partnership shall be reduced (but not below zero) by—

(1) The amount of any money distributed to such partner, and

(2) The amount of the basis to such partner of distributed property other. than money, as determined under section 732.

§ 1.733–1 *Basis of distributee partner's interest.* In the case of a distribution by a partnership to a partner other than in liquidation of a partner's entire interest, the adjusted basis to such partner of his interest in the partnership shall be reduced (but not below zero) by the amount of any money distributed to such partner and by the amount of the basis to him of distributed property other than money as determined under section 732 and § 1.732–1.

§ 1.734 *Statutory provisions; optional adjustment to basis of undistributed partnership property.*

SEC. 734. *Optional adjustment to basis of undistributed partnership property*—(a) *General rule.* The basis of partnership property shall not be adjusted as the result of a distribution of property to a partner unless the election, provided in section 754 (relating to optional adjustment to basis of partnership property), is in effect with respect to such partnership.

(b) *Method of adjustment.* In the case of a distribution of property to a partner, a partnership, with respect to which the election provided in section 754 is in effect, shall—

(1) Increase the adjusted basis of partnership property by—

(A) The amount of any gain recognized to the distributee partner with respect to such distribution under section 731 (a) (1), and

(B) In the case of distributed property to which section 732 (a) (2) or (b) applies, the excess of the adjusted basis of the distributed property to the partnership immediately before the distribution (as adjusted by section 732 (d)) over the basis of the distributed property to the distributee, as determined under section 732, or

(2) Decrease the adjusted basis of partnership property by—

(A) The amount of any loss recognized to the distributee partner with respect to such distribution under section 731 (a) (2), and

(B) In the case of distributed property to which section 732 (b) applies, the excess of the basis of the distributed property to the distributee, as determined under section 732, over the adjusted basis of the distributed property to the partnership immediately before such distribution (as adjusted by section 732 (d)).

(c) *Allocation of basis.* The allocation of basis among partnership properties where subsection (b) is applicable shall be made in accordance with the rules provided in section 755.

§ 1.734–1 *Optional adjustment to basis of undistributed partnership property*—(a) *General rule.* A partnership shall not adjust the basis of partnership property as the result of a distribution of property to a partner, unless the election provided in section 754 (relating to optional adjustment to basis of partnership property) is in effect.

(b) *Method of adjustment*—(1) *Increase in basis.* The adjustment provided under section 734 (b) with respect to basis of undistributed partnership property may not be made unless the election provided in section 754 is in effect. Where such election is in effect and a distribution of partnership property is made, whether or not in liquidation of the partner's entire interest in the partnership, the adjusted basis of the remaining partnership assets shall be increased by—

(i) The amount of any gain recognized under section 731 (a) (1) to the distributee partner, and

(ii) The excess of the adjusted basis to the partnership immediately before the distribution of any property distributed (as adjusted under section 732 (d)) over the basis under section 732 of such property to the distributee partner.

(2) *Decrease in basis.* Where the election provided in section 754 is in effect and a distribution is made in liquidation of a partner's entire interest, the partnership shall decrease the adjusted basis of the remaining partnership property by—

(i) The amount of loss, if any, recognized under section 731 (a) (2) to the distributee partner, and

(ii) In the case of distributed property to which section 732 (b) applies, the excess of the basis of the distributed property to the distributee, as determined under section 732, over the adjusted basis of such property to the partnership immediately before such distribution (as adjusted under section 732 (d))

(c) *Allocation of basis.* For allocation among the partnership properties of basis adjustments under section 734 (b) and paragraph (b) above, see section 755 and § 1.755–1.

§ 1.734–2 *Adjustment after distribution to transferee partner* (a) In the case of a distribution of property by the partnership to a partner who has obtained all or part of his partnership interest by transfer, the adjustments to basis provided in section 743 (b) and section 732 (d) shall be taken into account in applying the rules under section 734 (b) and § 1.734–1 (b) For determining the adjusted basis of distributed property to the partnership immediately before the distribution where there has been a prior transfer of a partnership interest with respect to which the election provided in section 754 or section 732 (d) is in effect, see § 1.732–2.

(b) (1) If a transferee partner in liquidation of his entire partnership interest receives a distribution of property (including money) with respect to which he has no special basis adjustment in exchange for his interest in property with respect to which he has a special basis adjustment and does not utilize his entire special basis adjustment in determining the basis of the distributed property to him under section 732, the unused special basis adjustment of the distributee shall be applied as an adjustment to the partnership basis of the property retained by the partnership and as to which the distributee did not use his special basis adjustment. The provisions of this subparagraph may be illustrated by the following example:

Example. Upon the death of his father, partner B acquires by inheritance a half-interest in partnership ABC. Partners A and C each have a one-quarter interest. The assets of the partnership consist of $100,000 in cash and real estate worth $100,000 with a basis of $10,000 to the partnership. Since the partnership had made the election under section 754 at the time of the transfer, partner B has a special basis adjustment of $45,000 under section 743 (b) with respect to his undivided half-interest in the real estate. The basis of B's partnership interest, in accordance with section 742, is $100,000. B retires from the partnership and receives $100,000 in cash in exchange for his entire interest. Since B has received no part of the real estate, his special basis adjustment of $45,000 will be allocated to the real estate, the remaining partnership property, and will increase its basis to the partnership to $55,000.

(2) The provisions of this paragraph do not apply to certain distributions treated as sales or exchanges under section 751 (b) (relating to unrealized receivables and substantially appreciated inventory items) See section 751 (b) and § 1.751–1 (b)

§ 1.735 *Statutory provisions; character of gain or loss on disposition of distributed property.*

SEC. 735. *Character of gain or loss on disposition of distributed property*—(a) *Sale or exchange of certain distributed property*—(1) *Unrealized receivables.* Gain or loss on the disposition by a distributee partner of unrealized receivables (as defined in section 751 (c)) distributed by a partnership, shall be considered gain or loss from the sale or exchange of property other than a capital asset.

(2) *Inventory items.* Gain or loss on the sale or exchange by a distributee partner of inventory items (as defined in section 751 (d) (2)) distributed by a partnership shall, if sold or exchanged within 5 years from the date of the distribution, be considered gain or loss from the sale or exchange of property other than a capital asset.

(b) *Holding period for distributed property.* In determining the period for which a partner has held property received in a distribution from a partnership (other than for purposes of subsection (a) (2)), there shall be included the holding period of the

partnership, as determined under section 1223, with respect to such property.

§ 1.735–1 *Character of gain or loss on disposition of distributed property*—(a) *Sale or exchange of distributed property*—(1) *Unrealized receivables.* Any gain realized or loss sustained by a partner on a sale or exchange or other disposition of unrealized receivables (as defined in section 751 (c)) received by him in a distribution from a partnership shall be considered gain or loss from the sale or exchange of property other than a capital asset.

(2) *Inventory items.* Any gain realized or loss sustained by a partner on a sale or exchange of inventory items (as defined in section 751 (d) (2)) received in a distribution from a partnership shall be considered gain or loss from the sale or exchange of property other than a capital asset if such inventory items are sold or exchanged within 5 years from the date of the distribution by the partnership. The character of any gain or loss from a sale or exchange by the distributee partner of such inventory items after 5 years from the date of distribution shall be determined as of the date of such sale or exchange by reference to the character of the assets in his hands at that date (inventory items, capital assets, property used in a trade or business, etc.)

(b) *Holding period for distributed property.* A partner's holding period for property distributed to him by a partnership shall include the period such property was held by the partnership, except for the purpose of determining the 5-year period decribed in section 735 (a) (2) and paragraph (a) (2) above. If the property has been contributed to the partnership by a partner, then the period that the property was held by such partner shall also be included. See section 1223 (2) For a partnership's holding period for contributed property, see § 1.723–1.

(c) *Effective date.* Section 735 (a) applies to any property distributed by a partnership to a partner after March 9, 1954. See section 771 (b) (2) and § 1.771–1 (b) (2)

§ 1.736 *Statutory provisions; payments to a retiring partner or a deceased partner's successor in interest.*

SEC. 736. *Payments to a retiring partner or a deceased partner's successor in interest*—(a) *Payments considered as distributive share or guaranteed payment.* Payments made in liquidation of the interest of a retiring partner or a deceased partner shall, except as provided in subsection (b), be considered—

(1) As a distributive share to the recipient of partnership income if the amount thereof is determined with regard to the income of the partnership, or

(2) As a guaranteed payment described in section 707 (c), if the amount thereof is determined without regard to the income of the partnership.

(b) *Payments for interest in partnership*—(1) *General rule.* Payments made in liquidation of the interest of a retiring partner or a deceased partner shall, to the extent such payments (other than payments described in paragraph (2)) are determined, under regulations prescribed by the Secretary or his delegate, to be made in exchange for the interest of such partner in partnership property, be considered as a distribution by the partnership and not as a distributive share or guaranteed payment under subsection (a).

(2) *Special rules.* For purposes of this subsection, payments in exchange for an interest in partnership property shall not include amounts paid for—

(A) Unrealized receivables of the partnership (as defined in section 751 (c)), or

(B) Good will of the partnership, except to the extent that the partnership agreement provides for a payment with respect to good will.

§ 1.736–1 *Payments to a retiring partner or a deceased partner's successor in interest*—(a) *Payments considered as distributive share or guaranteed payment.* (1) Payments which qualify under subparagraph (2) made by a partnership to a retiring partner or to the estate or other successor of a deceased partner in liquidation of the retiring or deceased partner's entire partnership interest are considered as—

(i) A distributive share of partnership income or a guaranteed payment under the rules contained in this paragraph, or

(ii) A payment for a partnership interest under the rules contained in paragraph (b)

If the amount of payment is determined with regard to the income of the partnership, then the amount thereof, to the extent that it is not considered a payment for the partner's interest in the partnership, shall be treated as a distributive share of partnership income to the recipient. See section 702 and § 1.702–1. If the amount of the payment is determined without regard to partnership income, then such amount, to the extent that it is not considered a payment for the partner's interest in the partnership, shall be treated as a guaranteed payment described in section 707 (c) and § 1.707–1 (c)

(2) Section 736 and this section apply only to certain payments made to a retiring partner or to a deceased partner's successor in interest in liquidation of such partner's entire interest in the partnership. A distribution of property does not qualify as a payment under section 736. Payments under section 736 must be in money and must consist of more than one payment in liquidation of such partner's entire partnership interest which is made in more than one partnership taxable year. To the extent that distributions in liquidation made to a retiring partner or to a deceased partner's successor in interest do not qualify as section 736 payments under the preceding sentence, gain or loss shall be recognized as provided in section 731 and § 1.731–1. Further, section 736 and this section apply only to payments made by the partnership to a retiring or deceased partner's successor in interest and do not apply to transactions between partners.

(3) Payments, to the extent considered as a distributive share of partnership income under section 736 (a) (1), are taken into account under section 702 and § 1.702–1 and thus reduce the amount of the distributive shares of the remaining partners. Payments, to the extent considered as guaranteed payments under section 736 (a) (2), are deductible by the partnership under section 162 (a) and are taxable as ordinary income to the recipient under section 61 (a). See section 707 (c) and § 1.707–1 (c)

(4) Payments made under section 736 (a) during the taxable year of the partnership shall be included in the income of the recipient for his taxable year within or with which such taxable year of the partnership ends. See section 706 (a) and § 1.706–1 (a).

(5) A retiring partner or a deceased partner's successor in interest receiving payments under section 736 is regarded as a partner until the entire interest of the retiring or deceased partner is liquidated. Therefore, if one of the members of a two-man partnership retires under a plan whereby he is to receive payments under section 736, the partnership will not be considered terminated since the retiring partner continues to hold a partnership interest in the partnership until his entire interest is liquidated. Similarly, if a partner in such a partnership dies, and his estate or other successor in interest receives payments under section 736, the partnership shall not be considered to have terminated upon the death of the partner but shall terminate when the entire interest of the decedent is liquidated. See section 708 (b) and § 1.708–1 (b).

(b) *Payments for interest in partnership.* (1) Payments made in liquidation of the entire interest of a retiring partner or deceased partner shall, to the extent made in exchange for such partner's interest in partnership property, be considered as a distribution by the partnership and not as a distributive share or guaranteed payment under section 736 (a) and paragraph (a) above, except as provided in subparagraphs (2) (3) and (4) below. The valuation placed by agreement of the partners upon a partner's interest in partnership property will be accepted to the extent that such valuation is reasonable. Gain or loss with respect to distributions under section 736 (b) and this paragraph will be recognized to the distributee to the extent provided in section 731 and § 1.731–1.

(2) Payments made to a retiring partner or to the successor in interest of a deceased partner for his interest in unrealized receivables of the partnership, as defined in section 751 (a), shall not be considered as made in exchange for such partner's interest in partnership property. Such payments shall be treated as payments under section 736 (a) and paragraph (a) of this section.

(3) For the purposes of section 736 (b) and this paragraph, payments made to a retiring partner or to a successor in interest of a deceased partner in exchange for the interest of such partner in partnership property shall not include any amount paid for the partner's share of good will of the partnership, except to the extent that the partnership agreement provides for a reasonable payment with respect to such good will. Such payments shall be considered as payments under section 736 (a) and paragraph (a) of this section. To the extent that the partnership agreement provides for a reasonable payment with respect to good will, such payments shall be

treated under section 736 (b) and this paragraph. The valuation placed upon good will by the agreement of the partners, whether specific in amount or determined in accordance with an agreed method of evaluation, shall be presumed correct if the amount so attributable does not exceed the reasonable value of the partner's share of partnership good will.

(4) Payments made to a retiring partner or to a successor in interest of a deceased partner for his interest in substantially appreciated inventory items, as defined in section 751 (d) shall not be considered as made in exchange for such partner's interest in partnership property for the purposes of section 736 (b) and this paragraph. Such payments shall be subject to the rules provided in section 751 (b) and § 1.751–1 (b)

(5) (i) Where payments made under section 736 are received during the taxable year, the recipient must segregate that portion of each such payment which is determined to be in exchange for the partner's interest in partnership property and treated as a distribution under section 736 (b) from that portion treated as a distributive share or guaranteed payment under section 736 (a) If a fixed amount (whether or not supplemented by any additional amounts) is to be received over a fixed number of years, the portion thereof to be treated as a distribution under section 736 (b) for the taxable year shall be equal to the total value of the interest of the retiring or deceased partner in partnership property, divided by the number of years over which the payments are to be made. The balance, if any, of such amount received in the same taxable year shall be treated as a distributive share or a guaranteed payment under section 736 (a) (1) or (2) However, if the total amount received in any one year is less than the amount considered as a distribution for that year under this subdivision, then any unapplied portion shall be added to the portion of the payments for the following year or years which are to be treated as a distribution under section 736 (b) For example, retiring partner W who is entitled to an annual payment of $6,000 for 10 years for his interest in partnership property, receives only $3,500 in 1955. In 1956, he receives $10,000. Of this amount, $8,500 ($6,000 plus $2,500 from 1955) is treated as a distribution under section 736 (b) for 1956; $1,500 as a payment under section 736 (a)

(ii) If the retiring or deceased partner's successor in interest receives payments which are not fixed in amount, such payments shall first be treated as payments in exchange for his interest in partnership property under section 736 (b) to the extent of the value of that interest and, thereafter, as payments under section 736 (a)

(iii) The amount of any gain or loss with respect to a retiring or deceased partner's interest in partnership property for each year of payment with respect to that interest shall be measured by the difference between—

(a) The amount treated as a distribution under section 736 (b) in that year, and

(b) The portion of the adjusted basis of the partner for his partnership interest attributable to such distribution (i. e., the amount which bears the same proportion to the partner's total adjusted basis for his partnership interest as the amount distributed under section 736 (b) in that year bears to the total amount to be distributed under section 736 (b))

(6) The provisions of this paragraph may be illustrated by the following examples:

Example (1). Partnership ABC is a personal service partnership and its balance sheet is as follows:

ASSETS

	Adjusted basis per books	Market value
Cash	$13,000	$13,000
Unrealized receivables	0	30,000
Fixed assets	20,000	23,000
Total	33,000	66,000

LIABILITIES AND CAPITAL

	Per books	Value
Liabilities	$3,000	$3,000
Capital:		
A	10,000	21,000
B	10,000	21,000
C	10,000	21,000
Total	33,000	66,000

Partner A retires from the partnership in accordance with an agreement whereby he is to receive $10,000 a year for 3 years, a total of $30,000, for his partnership interest. The value of A's interest in partnership property, for purposes of section 736 (b), is $12,000 (one-third of $36,000, the sum of $13,000 cash and $23,000, the fair market value of fixed assets). The unrealized receivables are not included in A's interest in partnership property under section 736 (b). Since the basis of A's interest is $11,000 ($10,000 plus $1,000, his share of partnership liabilities), he will realize a capital gain of $1,000 ($12,000 minus $11,000) on the disposition of his interest in partnership property. The balance to be received by him, $18,000 ($30,000 minus $12,000) constitutes payments under section 736 (a) and is taxable to A as ordinary income. The $10,000 A receives in each of the 3 years is to be allocated as follows: $4,000 as payments for his interest in partnership property (one-third of the total payment of $12,000), and the balance, $6,000, as guaranteed payments under section 736 (a) (2). Of the $4,000 attributable to A's interest in partnership property, $333 is capital gain (one-third of the total capital gain of $1,000), and $3,667 is a return of capital. The partnership will be entitled to a deduction of $6,000 during each of the 3 years for the guaranteed payments to A.

Example (2). Assume the same facts as in example (1) except that the agreement between the partners provides for payments to A for 3 years of a percentage of annual income instead of a fixed amount. All payments received by A up to $12,000 shall be treated under section 736 (b) as payments for A's interest in partnership property. Any payments in excess of $12,000 shall be treated as a distributive share of partnership income to A under section 736 (a) (1).

(c) *Cross reference.* See section 753 and § 1.753–1 for payments under section 736 (a) and paragraph (a) of this section made to a successor in interest of a decedent partner which are considered income in respect of a decedent under section 691.

Transfers of Interests in a Partnership

§ 1.741 *Statutory provisions; recognition and character of gain or loss on sale or exchange.*

SEC. 741. *Recognition and character of gain or loss on sale or exchange.* In the case of a sale or exchange of an interest in a partnership, gain or loss shall be recognized to the transferor partner. Such gain or loss shall be considered as gain or loss from the sale or exchange of a capital asset, except as otherwise provided in section 751 (relating to unrealized receivables and inventory items which have appreciated substantially in value).

§ 1.741–1 *Recognition and character of gain or loss on sale or exchange.* (a) The sale or exchange of an interest in a partnership shall, unless section 751 (relating to unrealized receivables and substantially appreciated inventory items) applies, be treated as the sale or exchange of a capital asset, resulting in capital gain or loss measured by the difference between the amount realized and the adjusted basis of the partnership interest as determined under section 705 and § 1.705–1. Where, however, the provisions of section 751 require the recognition of ordinary income or loss with respect to a portion of the amount realized from such sale or exchange, the amount realized shall be reduced by the amount attributable under section 751 to unrealized receivables and substantially appreciated inventory items, and the adjusted basis of the transferor partner's interest in the partnership shall be reduced by the portion of such basis attributable to such unrealized receivables and substantially appreciated inventory items. See section 751 and § 1.751–1.

(b) Section 741 shall apply whether the partnership interest is sold to one or more members of the partnership or to one or more persons who are not members of the partnership. Section 741 shall also apply where the sale of the partnership interest results in a termination of the partnership under section 708 (b) and § 1.708–1 (b) Thus, the provisions of section 741 shall be applicable (1) to the transferor partner in a two-man partnership when he sells his interest to the other partner, and (2) to all the members of a partnership when they sell their interests to one or more persons outside the partnership.

(c) See § 1.721–1 (b) for recognition of ordinary income where interest in partnership capital is obtained as compensation for services.

§ 1.742 *Statutory provisions; basis of transferee partner's interest.*

SEC. 742. *Basis of transferee partner's interest.* The basis of an interest in a partnership acquired other than by contribution shall be determined under part II of subchapter O (sec. 1011 and following).

§ 1.742–1 *Basis of transferee partner's interest.* The unadjusted basis to a transferee partner of an interest in a

partnership shall be determined under the general basis rules for property provided by part II of subchapter O (sections 1011 to 1022, inclusive) Thus, the basis of a purchased interest will be its cost. The basis of an interest acquired from a decedent partner will be the fair market value of the interest at death or the optional valuation date, reduced by any amount which is considered income in respect of a decedent under section 691. See section 722 and § 1.722–1 for basis of contributing partner's interest.

§ 1.743 *Statutory provisions; optional adjustment to basis of partnership property.*

SEC. 743. *Optional adjustment to basis of partnership property*—(a) *General rule.* The basis of partnership property shall not be adjusted as the result of a transfer of an interest in a partnership by sale or exchange or on the death of a partner unless the election provided by section 754 (relating to optional adjustment to basis of partnership property) is in effect with respect to such partnership.

(b) *Adjustment to basis of partnership property.* In the case of a transfer of an interest in a partnership by sale or exchange or upon the death of a partner, a partnership with respect to which the election provided in section 754 is in effect shall—

(1) Increase the adjusted basis of the partnership property by the excess of the basis to the transferee partner of his interest in the partnership over his proportionate share of the adjusted basis of the partnership property, or

(2) Decrease the adjusted basis of the partnership property by the excess of the transferee partner's proportionate share of the adjusted basis of the partnership property over the basis of his interest in the partnership.

Under regulations prescribed by the Secretary or his delegate, such increase or decrease shall constitute an adjustment to the basis of partnership property with respect to the transferee partner only. A partner's proportionate share of the adjusted basis of partnership property shall be determined in accordance with his interest in partnership capital and, in the case of an agreement described in section 704 (c) (2) (relating to effect of partnership agreement on contributed property), such share shall be determined by taking such agreement into account. In the case of an adjustment under this subsection to the basis of partnership property subject to depletion, any depletion allowable shall be determined separately for the transferee partner with respect to his interest in such property.

(c) *Allocation of basis.* The allocation of basis among partnership properties where subsection (b) is applicable shall be made in accordance with the rules provided in section 755.

§ 1.743–1 *Optional adjustment to basis of partnership property*—(a) *General rule.* The basis of partnership property shall not be adjusted as the result of a transfer of an interest in a partnership, either by sale or exchange or as a result of the death of a partner, unless the election provided by section 754 (relating to optional adjustment to basis of partnership property) is in effect with respect to the partnership.

(b) *Adjustment to basis of partnership property*—(1) *Determination of adjustment.* In the case of a transfer of an interest in a partnership, either by sale or exchange or as a result of the death of a partner, a partnership as to which the election under section 754 is in effect shall—

(i) Increase the adjusted basis of partnership property by the excess of the transferee's basis for his partnership interest over his proportionate share of the adjusted basis to the partnership of all partnership property, or

(ii) Decrease the adjusted basis of partnership property by the excess of the transferee partner's proportionate share of the adjusted basis of all partnership property over his basis for his partnership interest.

The amount of the increase or decrease constitutes an adjustment affecting the basis of partnership property with respect to the transferee partner only. Thus, for purposes of depreciation, depletion, gain or loss, and in the case of distributions, the transferee partner will have a special basis for those partnership properties which are adjusted under section 743 (b) and this paragraph, which basis is more or less than his proportionate share of the common partnership basis, i. e., the adjusted basis of such properties to the partnership. A partner's proportionate share of the adjusted basis of partnership property is determined in accordance with his interest in partnership capital (including his proportionate share of partnership liabilities) Where an agreement with respect to contributed property is in effect under section 704 (c) (2) and § 1.704–1 (c), such agreement shall be taken into account in determining a partner's proportionate share of the adjusted basis of partnership property. For example, if a partner's interest in partnership capital is one-third, his proportionate share of the adjusted basis of partnership property will, in general, be one-third of such basis. The provisions of this paragraph may be illustrated by the following examples:

Example (1). A is a member of partnership ABC in which all partners have equal interests in capital and profits. The partnership had made the election under section 754, relating to the optional adjustment to the basis of partnership property. A dies and his interest passes to his son S. The balance sheet of the partnership at the date of A's death shows the following:

ASSETS

	Adjusted basis per books	Market value
Cash	$5,000	$5,000
Accounts receivable	10,000	10,000
Inventory	20,000	21,000
Depreciable assets	20,000	40,000
Total	55,000	76,000

LIABILITIES AND CAPITAL

	Per books	Value
Liabilities	$10,000	$10,000
Capital:		
A	15,000	22,000
B	15,000	22,000
C	15,000	22,000
Total	55,000	76,000

The amount of the adjustment under section 743 (b) is determined by comparing the basis of the transferee's interest in the partnership with his proportionate share of the adjusted basis of partnership property. Under section 742, the basis of S's interest is $25,333 (the fair market value of A's interest at his death, $22,000, plus $3,333, his proportionate share of partnership liabilities). S's proportionate share of the adjusted basis of partnership property is $18,333, i. e., 1/3 of $45,000, the total adjusted basis of partnership property reduced by liabilities ($55,000 minus $10,000) plus $3,333 (S's proportionate share of partnership liabilities). The amount to be added to the basis of partnership property is $7,000, the difference between $25,333 and $18,333. This amount will be allocated to partnership properties in accordance with the rules set forth in section 755 and § 1.755–1.

Example (2). D is a member of partnership DEF in which the partners share equally in profits. The partnership has made the election under section 754. D dies and his interest passes to W, his widow. The balance sheet of the partnership at the date of D's death shows the following:

ASSETS

	Adjusted basis per books	Market value
Cash	$7,000	$7,000
Accounts receivable	10,000	10,000
Inventory	20,000	24,000
Depreciable assets	20,000	40,000
Total	57,000	81,000

LIABILITIES AND CAPITAL

	Per books	Value
Liabilities	$10,000	$10,000
Capital:		
D	18,000	26,000
E	15,000	23,000
F	14,000	22,000
Total	57,000	81,000

The amount of the adjustment under section 743 (b) is determined by comparing the basis of the transferee's interest in the partnership with his proportionate share of the adjusted basis of partnership property. Under section 742, the basis of W's interest is $29,333, that is, $26,000, her share of the fair market value of partnership property, plus $3,333, her proportionate share of partnership liabilities. W's proportionate share of the adjusted basis of partnership property is $21,333 (1/3 of $47,000, the total adjusted basis of partnership property reduced by liabilities ($57,000 minus $10,000), plus $3,333 her proportionate share of partnership liabilities). The amount to be added to the basis of partnership property is $8,000, the difference between $29,333 and $21,333. This amount will be allocated to partnership properties in accordance with the rules set forth in section 755 and § 1.755–1.

Note that in the above examples the amount of the adjustment does not depend upon the adjusted basis to the transferor for his interest in partnership capital. The amount of the adjustment is the same whether the transferee acquires an interest by purchase or inheritance.

(2) *Determination of partner's proportionate share of adjusted basis of partnership property.* (i) Under the provisions of section 743 (b) a partner's proportionate share of the adjusted

basis of partnership property shall be determined by taking into account the effect of any partnership agreement with respect to contributed property as described in section 704 (c) (2) This rule may be illustrated by the following examples:

Example (1). A, B, and C form partnership ABC, to which A contributes property X, land worth $1,000 with an adjusted basis to him of $400, and B and C each contributes $1,000 in cash. Each partner has credited to him in the books of the partnership $1,000 as his capital contribution. The partners share in profits equally. During the partnership's first taxable year, property X appreciates in value to $1,300. A sells his one-third interest in the partnership to D for $1,100, and the partnership makes the election under section 754. There is no agreement under section 704 (c) (2) in effect. The adjusted basis of the partnership property is increased with respect to D by the excess of his basis for his partnership interest, $1,100, over his proportionate share of the adjusted basis of partnership property, $800 (⅓ of $2,400, the total adjusted basis of partnership property). The amount of the adjustment, therefore, is $300 ($1,100 minus $800), which is an increase in the basis of partnership property with respect to D only. This special basis adjustment will be allocated to property X. (See section 755 and § 1.755–1.) If X is sold for $1,600, the gain to the partnership is $1,200 ($1,600 received, less the adjusted partnership basis of $400 for property X). Thus, each partner's distributive share of the gain on the sale is $400. However, D's distributive share of the gain is $400, reduced by $300, his special basis adjustment with respect to property X, leaving him with a recognized gain of $100. If D purchased his interest from B or C, the partners who contributed cash, D's adjustment under section 743 (b) would also be $300, computed in exactly the same manner as in the case of a purchase from A.

Example (2). Assume that partnership ABC, described in example (1), has an agreement under section 704 (c) (2) with respect to property X, stating that upon the sale of that property any gain, to the extent attributable to the precontribution appreciation of $600 (the difference between its value, $1,000, and its basis, $400, at the time of the contribution) is to be allocated entirely to A, who contributed property X. Upon the purchase of A's interest by D for $1,100, the computation of D's special basis would differ from that indicated in example (1) as follows: Under the partnership agreement, A's share of the $2,400 adjusted basis of partnership property is $400 (his basis for property X prior to its contribution to the partnership), and B's and C's share is $1,000 each (the amount of the cash investment of each). The amount of the increase to D in the adjusted basis of partnership property under section 743 (b) (1) is $700 (the excess of $1,100, D's cost basis for his interest, over $400, A's share of the adjusted basis of partnership property to which D succeeds). This amount constitutes an adjustment to the basis of partnership property with respect to D only. If X is sold by the partnership for $1,600, the gain is $1,200 ($1,600 less the adjusted partnership basis of $400). Under the partnership agreement, $600 of this gain, which is attributable to precontribution appreciation in value, is allocable to D, who is A's successor. The remaining $600 gain is not subject to the agreement and is allocable to the partners equally, $200 each. D's distributive share of the partnership gain is thus $600 plus $200, or $800. However, D has a special basis of $700 under section 743 (b) which reduces his gain from $800 to $100. B and C each has a gain of $200, which is unaffected by the transfer of A's interest to D.

Example (3). Assume the same facts as in example (2), except that D has purchased his interest from B instead of from A. His special basis adjustment for partnership property in this case differs from that where he had purchase his interest from A, because of the effect of the agreement under section 704 (c) (2). In this case, D is a successor to B, whose share of the adjusted basis of partnership property is $1,000, instead of A, whose share is $400. As a result, the adjustment under section 743 (b) (1) is the excess of D's cost basis for his interest, $1,100, over his proportionate share of the adjusted basis of partnership property, $1,000, or $100. In this case, if property X is sold for $1,600, the partnership gain is $1,200 ($1,600 less the adjusted partnership basis of $400). Of this gain, $600, representing precontribution appreciation, is allocable to A under the partnership agreement. The remaining $600 is allocable in the amount of $200 to each partner. Since D has a special transferee basis of $100 under section 743 (b), his gain is reduced from $200 to $100.

(ii) If a nontransferee partner receives a distribution of property with respect to which a transferee partner has a special basis adjustment, the property will have a basis to the partnership consisting only of its common basis shared by all the partners. The special basis adjustment of the transferee partner will not be taken into account. However, the special basis adjustment of the transferee partner will be reallocated to remaining partnership property of a like kind or, if the transferee partner receives a distribution of like property, to such distributed property. If a transferee partner receives a distribution of property with respect to which he has a special basis adjustment, such property will have a basis consisting of its common basis to all the partners, increased or decreased by the transferee partner's special basis adjustment. If the transferee partner at the same time relinquishes his interest in other property of a like kind with respect to which he also has a special basis adjustment, he will be permitted further to adjust the basis of the property received by his special basis adjustment with respect to the interest relinquished in such other like property. Any property in which a transferee partner has relinquished his special basis adjustment may remain in the partnership or may be distributed to other partners. For the purposes of this section, like property means property of the same class, that is, stock in trade, property used in the trade or business, capital assets, etc. For certain adjustments to the basis of remaining partnership property after a distribution to a transferee partner, see § 1.734–2 (b) The provisions of this subdivision may be illustrated by the following example:

Example. C is a transferee partner in partnership BC. The partnership owns, among other assets, X, a depreciable asset with a common basis to the partnership of $1,000 and a special basis adjustment to C of $200, and Y, another depreciable asset with a common basis of $800 and a special basis adjustment to C of $300. B and C agree that B will receive a distribution of Y, and C will receive a distribution of X, with all other property to remain in the partnership. With respect to B, the partnership basis of property Y is $800, the common partnership basis. Y will, therefore, have a basis of $800 in B's hands under section 732 (a) which provides for the use of a carryover basis in the case of current distributions. With respect to C, however, the partnership basis of property X is $1,500, the common partnership basis of $1,000, plus C's special basis adjustment of $200 for property X, plus C's additional special basis adjustment of $300 for property Y in which he has relinquished his interest.

(iii) Where an adjustment is made under section 743 (b) to the basis of partnership property subject to depletion, any depletion allowable shall be determined separately for the transferee partner with respect to his interest in such property. This rule may be illustrated by the following example:

Example. A, B, and C each contribute $5,000 in cash to form partnership ABC, which purchases oil property for $15,000. C subsequently sells his partnership interest to D for $100,000. The difference between D's basis, $100,000, and his proportionate share of the basis of partnership property, $5,000, or $95,000, is a special basis adjustment for the oil property with respect to D. Assume that the depletion allowance computed under the percentage method would be $21,000 for the taxable year. Thus, each partner would be entitled to a $7,000 allowance. However, under the cost depletion method, at an assumed rate of 10 percent the allowance with respect to the one-third interest of A and B in the oil property, each of which has a basis of $5,000, is $500, and the allowance with respect to D's one-third interest which has a basis to him of $100,000 ($5,000, plus D's special basis adjustment of $95,000) is $10,000. With respect to partners A and B, the percentage depletion is greater than cost depletion and each can deduct $7,000 based on the percentage depletion method. With respect to D, the transferee partner, the cost depletion method will result in a greater allowance and D can, therefore, deduct $10,000 based on cost depletion.

(iv) Where there has been more than one transfer of the same partnership interest, any special basis adjustment under section 743 (b) of the last transferee shall be determined with respect to the partnership's common basis for its property without regard to any special basis adjustment under section 743 (b) of any intermediate transferee. For example, A, B, and C form a partnership. A and B each contributes $1,000 in cash and C contributes land with a basis and value of $1,000. When the land has appreciated in value to $1,300, A sells his interest to D for $1,100 (⅓ of $3,300, the value of the partnership property) D has a special basis adjustment of $100 with respect to the land under section 743 (b) (1) After the land has further appreciated in value to $1,600, D sells his interest to E for $1,200 (⅓ of $3,600, the value of the partnership property) Under section 743 (b) (1) E has a special basis adjustment of $200. This amount is determined without regard to any special basis adjustment that D may have had in the partnership assets.

(c) *Allocation of basis.* For the allocation of basis among partnership properties where section 743 (b) applies, see section 755 and § 1.755–1.

Provisions Common to Other Subparts

§ 1.751 *Statutory provisions; unrealized receivables and inventory items.*

SEC. 751. *Unrealized receivables and inventory items*—(a) *Sale or exchange of interest in partnership.* The amount of any money, or the fair market value of any property, received by a transferor partner in exchange for all or a part of his interest in the partnership attributable to—

(1) Unrealized receivables of the partnership, or

(2) Inventory items of the partnership which have appreciated substantially in value,

shall be considered as an amount realized from the sale or exchange of property other than a capital asset.

(b) *Certain distributions treated as sales or exchanges*—(1) *General rule.* To the extent a partner receives in a distribution—

(A) Partnership property described in subsection (a) (1) or (2) in exchange for all or a part of his interest in other partnership property (including money), or

(B) Partnership property (including money) other than property described in subsection (a) (1) or (2) in exchange for all or a part of his interest in partnership property described in subsection (a) (1) or (2),

such transactions shall, under regulations prescribed by the Secretary or his delegate, be considered as a sale or exchange of such property between the distributee and the partnership (as constituted after the distribution).

(2) *Exceptions.* Paragraph (1) shall not apply to—

(A) A distribution of property which the distributee contributed to the partnership, or

(B) Payments, described in section 736 (a), to a retiring partner or successor in interest of a deceased partner.

(c) *Unrealized receivables.* For purpose of this subchapter, the term "unrealized receivables" includes, to the extent not previously includible in income under the method of accounting used by the partnership, any rights (contractual or otherwise) to payment for—

(1) Goods delivered, or to be delivered, to the extent the proceeds therefrom would be treated as amounts received from the sale or exchange of property other than a capital asset, or

(2) Services rendered, or to be rendered.

(d) *Inventory items which have appreciated substantially in value*—(1) *Substantial appreciation.* Inventory items of the partnership shall be considered to have appreciated substantially in value if their fair market value exceeds—

(A) 120 percent of the adjusted basis to the partnership of such property, and

(B) 10 percent of the fair market value of all partnership property, other than money.

(2) *Inventory items.* For purposes of this subchapter the term "inventory items" means—

(A) Property of the partnership of the kind described in section 1221 (1),

(B) Any other property of the partnership which, on sale or exchange by the partnership, would be considered property other than a capital asset and other than property described in section 1231, and

(C) Any other property held by the partnership which, if held by the selling or distributee partner, would be considered property of the type described in subparagraph (A) or (B).

§ 1.751–1 *Unrealized receivables and inventory items*—(a) *Sale or exchange of interest in a partnership*—(1) *Character of amount realized.* To the extent that money or property received by a partner in exchange for all or part of his partnership interest is attributable to the value of his proportionate share of partnership unrealized receivables or substantially appreciated inventory items, the money or fair market value of the property received shall be considered an amount realized from the sale or exchange of property other than a capital asset. The remainder of the total amount realized on the sale or exchange is considered as realized from the sale or exchange of a capital asset under section 741. See § 1.741–1. For definition of unrealized receivables and inventory items which have appreciated substantially in value, see section 751 (c) and (d) and paragraphs (c) and (d) below.

(2) *Determination of gain or loss.* (i) In determining the amount of ordinary income or loss realized by a partner upon the sale or exchange of his interest in unrealized receivables or substantially appreciated inventory items, a portion of the partner's adjusted basis for his partnership interest must be allocated to his share of such receivables and inventory items. The amount to be allocated to such receivables and inventory items shall be his pro rata share of the partnership basis for such properties. If, however, the transferor partner had acquired his partnership interest in a transfer resulting in a special basis adjustment to him under section 743 (b), then his pro rata share of the common partnership basis for such property shall be adjusted by his special basis adjustment applicable to such property. The difference between the basis thus allocated to unrealized receivables and substantially appreciated inventory items and that portion of the amount realized attributable to such property shall be ordinary income or loss to the transferor. The difference between the remainder, if any, of the partner's adjusted basis for his partnership interest and the balance, if any, of the amount realized shall determine the transferor's capital gain or loss on the sale of his partnership interest.

(ii) If the transferor acquired his interest in a previous transfer but has no special basis adjustment under section 743 (b) with respect to partnership property because the election described in section 754 was not in effect, such partner may elect, on a subsequent sale or exchange of his interest within 2 years after he acquired such interest by transfer, to treat as the adjusted partnership basis of unrealized receivables and substantially appreciated inventory items the adjusted basis such items would have if the adjustment provided in section 743 (b) were in effect. In addition to the statement required under subparagraph (3) below, a transferee partner who elects under this subdivision shall submit with his income tax return for his taxable year in which he sells or exchanges his interest, a schedule setting forth the following information:

(*a*) The adjusted basis to him of his partnership interest (or such part thereof) acquired by transfer and the date of transfer;

(*b*) The adjusted basis to the partnership of his pro rata share of partnership unrealized receivables and substantially appreciated inventory items that are included in the interest sold or exchanged, the fair market value of such items and his pro rata share thereof, and the date of such sale or exchange;

(*c*) The amount of the special basis adjustment to be attributed under this subdivision to the unrealized receivables and substantially appreciated inventory items, and the computation of such amount; and

(*d*) The amount received by the transferor for his interest, the amount attributable to unrealized receivables and substantially appreciated inventory items and the ordinary income or loss recognized, and the amount attributable to other partnership property and the capital gain or loss recognized.

(3) *Statement required.* A transferor partner selling or exchanging all or part of his interest in a partnership shall submit with his income tax return for the taxable year in which the sale or exchange occurs a statement setting forth separately the following information:

(i) The amount of the transferor partner's adjusted basis for his partnership interest, and the portion thereof attributable to unrealized receivables and substantially appreciated inventory items; and

(ii) The amount of any money and the fair market value of any other property received or to be received for the transferred interest in the partnership, and the portion thereof attributable to unrealized receivables or substantially appreciated inventory items.

(b) *Certain distributions of property treated as sales or exchanges*—(1) *Distribution of unrealized receivables or substantially appreciated inventory items.* (i) To the extent that a partner receives in a current distribution or in a distribution in liquidation of his entire interest unrealized receivables or substantially appreciated inventory items of the partnership in exchange for all or a part of his interest in other partnership property (including money) the transaction shall be treated as a sale or exchange of such property between the distributee partner and the partnership as constituted after the distribution. The gain realized by the partnership on the transaction shall be treated as ordinary income and the amount thereof recognized to the partnership shall be measured by the difference between the adjusted basis to the partnership of the amount of unrealized receivables and substantially appreciated inventory items distributed to the partner, and the fair market value of the distributee partner's interest in other property of the partnership relinquished in exchange therefor. The distributee partner realizes capital gain or loss measured by the difference between his share of the adjusted basis of the property relinquished and the fair market value of the unrealized receivables or substantially appreciated inventory items received by him in exchange for the relinquished interest.

(ii) The rules of subdivision (i) shall not apply to a distribution to a partner of all or part of his proportionate share of partnership unrealized receivables or substantially appreciated inventory items where the distribution is not in exchange for his interest in other partnership property. If a distribution is, in part, a distribution of the distributee partner's proportionate share of such unrealized receivables or substantially appreciated inventory items and, in part, a distribution in exchange for the distributee partner's interest in other partnership property, an allocation shall be made for the purpose of applying section 751 (b) and this subparagraph to the distributee partner and the partnership.

(2) *Distribution of partnership property other than unrealized receivables or substantially appreciated inventory items.* To the extent that a partner receives, in a current distribution or in a distribution in liquidation of his entire interest, partnership property including money (other than unrealized receivables or substantially appreciated inventory items) in exchange for all or a part of his interest in partnership unrealized receivables and substantially appreciated inventory items, the transaction shall be treated as a sale or exchange of such property between the distributee partner and the partnership as constituted after the distribution. The gain realized by the partner on such transaction shall be ordinary income and the amount of such gain shall be measured by the excess of the fair market value of the assets distributed to him over his proportionate share of the adjusted basis of partnership unrealized receivables and substantially appreciated inventory items which are considered as sold or exchanged. The partnership will realize a capital gain or loss measured by the difference between the adjusted basis to the partnership of the assets exchanged and the fair market value of the distributee partner's interest in the unrealized receivables and substantially appreciated inventory items which the partnership acquires in the exchange.

(3) *Rules for application of this paragraph.* (i) The rules of this paragraph do not apply to the distribution to a partner of property which the distributee partner contributed to the partnership. The distribution of such property is governed by the rules set forth in sections 731–736, inclusive, relating to distributions by a partnership.

(ii) Payments made to a retiring partner or to a deceased partner's successor in interest shall not be treated as a sale or exchange between the partner and the partnership to the extent that such payments constitute a distributive share of partnership income or guaranteed payments under section 736 (a) and § 1.736–1 (a) However, to the extent that such payments are considered to be in exchange for an interest in partnership property under section 736 (b) section 751 (b) and this paragraph shall apply. Thus, a payment under section 736 (b) must be treated, if the inventory items of the partnership are substantially appreciated, as made in part for the distributee's interest in partnership substantially appreciated inventory items to the extent of the fair market value thereof, and in part for the distributee's interest in other partnership property. Payments for unrealized receivables of a partnership do not constitute payments for a partnership interest but are payments under section 736 (a) and no allocation under section 751 (b) need be made. See section 736 and § 1.736–1.

(iii) In determining the adjusted basis to a distributee partner of any unrealized receivables, substantially appreciated inventory items, or any other partnership property, any special basis adjustment arising under section 743 (b) with respect to that partner shall be taken into account. See section 743 (b) and § 1.743–1 (b) However, no special basis adjustment under section 732 (d) shall be taken into account for the purposes of applying section 751 (b) See section 732 (e)

(iv) A partnership which distributes to a partner unrealized receivables or substantially appreciated inventory items in exchange for his interest in other partnership property, or which distributes other property in exchange for all or a part of the partner's share of partnership unrealized receivables or substantially appreciated inventory items, shall submit with its return for the year of the distribution a statement showing the computation of the income, gain, or loss both to the partnership and to the distributee under the provisions of this paragraph. The distributee partner shall submit the statement required under paragraph (a) (3) of this section.

(c) *Unrealized receivables.* The term "unrealized receivables" as used in subchapter K, includes (1) any rights (contractual or otherwise) to payment for goods delivered or to be delivered, if such payment would be treated as received for property other than a capital asset, or (2) any rights arising out of services rendered or to be rendered. If such rights were previously includible in income under a method of accounting employed by the partnership, then to that extent their value shall not constitute unrealized receivables.

(d) *Inventory items which have substantially appreciated in value*—(1) *Substantial appreciation.* Partnership inventory items shall be considered to have appreciated substantially in value if, at the time of the distribution, the total fair market value of all the inventory items of the partnership exceeds 120 percent of the aggregate adjusted basis for such property in the hands of the partnership (without regard to any special basis adjustment of any partner) and, in addition, exceeds 10 percent of the fair market value of all partnership property other than money. The terms "inventory items which have appreciated substantially in value" or "substantially appreciated inventory items" refer to the aggregate of all partnership inventory items. These terms do not refer to specific partnership inventory items or to specific groups of such items. For example, any distribution of inventory items by a partnership the inventory items of which as a whole are substantially appreciated in value shall be a distribution of substantially appreciated inventory items for the purposes of section 751 (b) even though the specific inventory items distributed may not be appreciated in value. Similarly, if the aggregate of partnership inventory items are not substantially appreciated in value, a distribution of specific inventory items, the value of which is more than 120 percent of their adjusted basis for such property, will not constitute a distribution of substantially appreciated inventory items.

(2) *Inventory items.* The term "inventory items" as used in subchapter K includes the following types of property:

(i) Stock in trade of the partnership, or other property of a kind which would properly be included in the inventory of the partnership if on hand at the close of the taxable year, or property held by the partnership primarily for sale to customers in the ordinary course of its trade or business. See section 1221 (1)

(ii) Any other property of the partnership which, on sale or exchange by the partnership, would be considered property other than a capital asset and other than property described in section 1231.

(iii) Any other property held by the partnership which, if held by the partner selling his partnership interest or receiving a distribution described in section 751 (b) would be considered property described in subdivisions (i) or (ii) above.

(e) *Examples.* Application of the provisions of section 751 may be illustrated by the following examples:

Example (1). C buys B's interest in personal service partnership AB for $15,000, when the balance sheet of the firm (reflecting a cash receipts and disbursements method of accounting) is as follows:

ASSETS

	Adjusted basis per books	Market value
Cash	$3,000	$3,000
Loans receivable	10,000	10,000
Other assets	7,000	7,000
Unrealized receivables	0	12,000
Total	20,000	32,000

LIABILITIES AND CAPITAL

	Per books	Value
Liabilities	$2,000	$2,000
Capital:		
A	9,000	15,000
B	9,000	15,000
Total	20,000	32,000

Section 751 (a) applies to the sale. The total amount realized by B is $16,000, consisting of the cash received, $15,000, plus $1,000, B's share of the partnership liabilities assumed by C. See section 752. B's undivided half interest in the partnership property includes a half-interest in the partnership's unrealized receivables which are worth $12,000. Consequently, $6,000 of the $16,000 realized by B shall be considered received in exchange for B's interest in the

partnership attributable to its unrealized receivables (with zero basis) and shall constitute ordinary income to B. The remaining $10,000 realized by B is in exchange for a capital asset. B's basis for his partnership interest is $10,000, which includes $1,000, B's share of partnership liabilities. No portion of this basis is attributable to B's share of the unrealized receivables of the partnership since such property has a zero basis in the hands of the partnership. Thus, the entire $10,000 of B's basis is attributable to his interest in partnership property other than unrealized receivables and is applied against the $10,000 ($16,000 minus $6,000) realized on the sale of his interest. Therefore, B has no capital gain or loss. (If B's basis for his interest in partnership property, other than unrealized receivables, were $9,000, he would realize capital gain of $1,000. If his basis were $11,000, he would sustain a capital loss of $1,000.)

Example (2). Partnership ABC makes a distribution to partner C in liquidation of his entire interest in the partnership. At the time of the distribution, the balance sheet of the partnership, which uses the accrual method of accounting, is as follows:

ASSETS

	Adjusted basis per books	Market value
Cash	$10,000	$10,000
Accounts receivable	15,000	15,000
Inventory	30,000	39,000
Depreciable property	40,000	46,000
Total	95,000	110,000

LIABILITIES AND CAPITAL

	Per books	Value
Current liabilities	$5,000	$5,000
Mortgages payable	30,000	30,000
Capital:		
A	20,000	25,000
B	20,000	25,000
C	20,000	25,000
Total	95,000	110,000

The distribution received by C consists of $10,000 cash and depreciable property with a fair market value of $15,000 and an adjusted basis to the partnership of $15,000. The partnership has no unrealized receivables, but the dual test provided in section 751 (d) (1) must be applied to determine whether the inventory items of the partnership have, in the aggregate, appreciated substantially in value. The fair market value of all partnership inventory items, $39,000, exceeds by more than 120 percent the $30,000 adjusted basis of such items to the partnership. The fair market value of the inventory, $39,000, also exceeds 10 percent of the fair market value of all partnership property other than money (10 percent of $100,000, or $10,000). Therefore, the partnership inventory items have substantially appreciated in value and the transaction is governed by section 751 (b). C has received partnership property (including money) other than unrealized receivables and substantially appreciated inventory items in exchange for his interest in substantially appreciated inventory items. C's share of the fair market value of partnership inventory is $13,000 (one-third of $39,000). Thus, $13,000 of the total amount received by C on the distribution is considered as realized by C on the sale or exchange of inventory items. C's basis for his share of partnership inventory items is $10,000 (one-third of $30,000, the basis of such inventory items to the partnership). C realizes $3,000 ($13,000 minus $10,000) in ordinary income under section 751 (b), and the partnership (as constituted after C's retirement) will increase the basis of its inventory by $3,000 to $13,000 to reflect the cost of purchasing C's share of inventory items. Since, under section 751 (b), C is regarded as having sold to the partnership for $18,000 his share of inventory items with an adjusted basis to him of $10,000, this portion of the distribution is treated as a sale or exchange of property and is not subject to the distribution rules provided for partnerships under sections 731–736, inclusive. Therefore, the basis of C's partnership interest must be reduced by $10,000, and $13,000 of the amount distributed to C by the partnership is regarded as an amount realized by C on the sale of the interest in inventory items. Accordingly, C's basis for his partnership interest is $21,666 ($20,000, C's basis for his interest not taking liabilities into account, plus $11,666, his share of partnership liabilities, or $31,666, reduced by $10,000, the basis of his interest in inventory items considered as sold by C to the partnership). The total amount treated as a distribution to C is $23,666, determined as follows: $15,000, the fair market value of the depreciable property, plus $8,666 regarded as money received ($10,000 cash, plus $11,666, his share of partnership liabilities assumed by the partnership, treated as a distribution of money under section 752 (b), or $21,666; this amount is reduced by $13,000, the amount considered as paid by the partnership in purchase of C's interest in inventory items). The basis to C of the depreciable property received by him in the distribution is determined under section 732 (c). The basis of C's partnership interest, $21,666, is decreased by $8,666 money received. This balance of $13,000 is the basis under section 732 (c) of the depreciable property distributed to C. (The adjusted basis of this property to the partnership had been $15,000. If the partnership makes or has made an election under section 754, the adjustment described in section 734 (b) shall be made, and the partnership will increase the basis of the remaining partnership depreciable property by $2,000, the excess of the adjusted basis of the distributed depreciable property to the partnership immediately before the distribution, $15,000, over its basis to the distributee, $13,000.) After the distribution to C, the balance sheet of the partnership appears as follows:

ASSETS

	Adjusted basis per books	Market value
Cash	0	0
Accounts receivable	$15,000	$15,000
Inventory	33,000	39,000
Depreciable property	27,000	31,000
Total	75,000	85,000

LIABILITIES AND CAPITAL

	Per books	Value
Current liabilities	$5,000	$5,000
Mortgages payable	30,000	30,000
Capital:		
A	20,000	25,000
B	20,000	25,000
Total	75,000	85,000

Example (3). Assume that the distribution to partner C in example (2) in liquidation of his entire interest in partnership ventory received by him, $6,500 ($19,500 worth of partnership inventory. Since C's proportionate share of the fair market value of partnership inventory worth $39,000 is $13,000, the excess of the value of the inventory received by him, $6,500 ($19,500 minus $13,000) is considered as a sale by the partnership (as constituted after the distribution) of $6,500 worth of inventory for C's interest in other partnership assets. Since the inventory considered sold by the partnership is one-sixth ($6,500/$39,000) of the total fair market value of partnership inventory, the basis attributable to such inventory is $5,000 (one-sixth of $30,000, the total partnership basis for its inventory). Thus, the partnership realizes $1,500 ($6,500 minus $5,000) ordinary income on the transaction. The basis to C of the $19,500 worth of inventory distributed to him is $16,500 ($10,000, C's basis for his share of partnership inventory, plus $6,500, the fair market value of the inventory acquired from the partnership in exchange for C's interest in other partnership property). C has realized a capital gain of $2,000 on the transaction, computed as follows:

C received in excess of his interest in:	
Inventory items—$19,500 minus $13,000 (the value of his share) or	$6,500
Cash—$5,500 minus $3,333 (the value of his share) or	2,167
Liabilities assumed by the partnership—⅓ of $35,000 or	11,666
Total	20,333
C relinquished his interest in:	
Accounts receivable—⅓ of $15,000 or	5,000
Depreciable property—⅓ of $40,000 or	13,333
Total	18,333
C's capital gain is $20,333 minus $18,333 or	2,000

(f) *Effective date.* Section 751 applies to gain or loss to a seller, distributee, or partnership in the case of a sale, exchange, or distribution occurring after March 9, 1954. For the purpose of applying this paragraph in the case of a taxable year beginning before January 1, 1955, a partnership or a partner may elect to treat as applicable any other section of subchapter K. Any such election shall be made by a statement submitted not later than the time prescribed by law for the filing of the return for such taxable year, or submitted within 90 days after the promulgation of the regulations under this section, whichever date is later. See section 771 (b) (3) and § 1.771–1 (b) (3)

§ 1.752 *Statutory provisions; treatment of certain liabilities.*

SEC. 752. *Treatment of certain liabilities*—(a) *Increase in partner's liabilities.* Any increase in a partner's share of the liabilities of a partnership, or any increase in a partner's individual liabilities by reason of the assumption by such partner of partnership liabilities, shall be considered as a contribution of money by such partner to the partnership.

(b) *Decrease in partner's liabilities.* Any decrease in a partner's share of the liabilities of a partnership, or any decrease in a partner's individual liabilities by reason of the assumption by the partnership of such individual liabilities, shall be considered as a distribution of money to the partner by the partnership.

(c) *Liability to which property is subject.* For purposes of this section, a liability to which property is subject shall, to the extent of the fair market value of such property, be considered as a liability of the owner of the property.

(d) *Sale or exchange of an interest.* In the case of a sale or exchange of an interest in a partnership, liabilities shall be treated in the same manner as liabilities in connection with the sale or exchange of property not associated with partnerships.

§ 1.752–1 *Treatment of certain liabilities*—(a) *Increase in partner's liabilities.* (1) Where the liabilities of the partnership are increased, and each partner's share of such liabilities is thereby increased, the amount of the increase shall be treated as a pro rata contribution of money by the partners to the partnership. For example, partnership AB borrows $1,000. If A and B are equal partners, the basis of the partnership interest of each is increased by $500 as though each had contributed this amount in cash.

(2) Any increase in the partner's individual liabilities because of the assumption by him of partnership liabilities shall also be considered as a contribution of money by him to the partnership. For example, partner A receives a distribution from partnership AB of real property having an adjusted basis to the partnership of $1,000 and subject to a mortgage of $400. The distributee partner assumes the mortgage. Under the provisions of sections 733 (2) and 732 (a) (1) the basis of A's partnership interest is decreased after the distribution in the amount of $1,000. However, the basis of A's partnership interest is increased under sections 752 (a) and 722 by $200, which is that portion of the mortgage formerly attributable to partner B and reflected in his basis and which has now been assumed as an individual liability by partner A. (The remaining $200 of the mortgage assumed by A was already reflected in the basis of his partnership interest.)

(b) *Decrease in partner's liabilities.* (1) Where the liabilities of a partnership are decreased, and each partner's share of such liabilities is thereby decreased, the amount of the decrease shall be treated as a pro rata distribution of money to the partner by the partnership. For example, partnership AB in which A and B are equal partners repays an obligation of $10,000. The repayment reduces each partner's pro rata share of partnership liabilities by $5,000 and is considered a distribution which reduces the basis of each partner's interest in the partnership by that amount.

(2) Where a partnership assumes the personal liabilities of a partner or a liability to which property owned by such partner is subject (see paragraph (c) below) the amount of the decrease in such partner's liabilities is treated as a distribution of money by the partnership to such partner. For example, partner A contributes property with a basis of $1,000 to partnership AB in exchange for a one-half interest in the partnership. The property is subject to a mortgage of $150, which is assumed by the partnership. The basis of A's partnership interest is $925, computed as follows: $1,000, A's basis for the contributed property, reduced by $75, one-half of A's original liability of $150 now attributable to B and reflected in B's basis under the provisions of paragraph (a) above. One-half of A's original $150 liability, $75, is still attributable to him and is reflected in the basis of the partnership interest.

(c) *Liability to which property is subject.* Where property subject to a liability is contributed by a partner to a partnership, or distributed by a partnership to a partner, the amount of the liability shall, to an extent not exceeding the fair market value of the property be considered as a liability assumed by the transferee. For example, A contributes property with a basis to him of $1,000 to equal partnership AB. The property is subject to a mortgage of $2,500 and its value exceeds $2,500. Under paragraph (b), A will be treated as receiving a distribution in money of $1,250, one-half of the liability of $2,500 assumed by the partnership. Since the basis of A's partnership interest is $1,000 (the basis of the property contributed by him) the distribution to him of $1,250 results in a capital gain to him of $250 under section 731 (a) and § 1.731–1 (a)

(d) *Sale or exchange of an interest.* Where there is a sale or exchange of an interest in a partnership, liabilities shall be treated in the same manner as liabilities in connection with the sale or exchange of property not associated with partnerships. For example, if a partner sells his interest in a partnership for $750 cash and at the same time transfers to the purchaser his pro rata share of partnership liabilities amounting to $250, the amount realized by the seller on the transaction is $1,000.

§ 1.753 *Statutory provisions; partner receiving income in respect of decedent.*

SEC. 753. *Partner receiving income in respect of decedent.* The amount, includible in the gross income of a successor in interest of a deceased partner under section 736 (a) shall be considered income in respect of a decedent under section 691.

§ 1.753–1 *Partner receiving income in respect of decedent*—(a) *General.* All payments coming within the provisions of section 736 (a) made by a partnership to the estate or other successor in interest of a deceased partner are considered payments of income in respect of the decedent under section 691. The estate or other successor in interest of a deceased partner shall be considered to have received income in respect of a decedent to the extent that amounts are paid by a third person in exchange for rights to future payments under section 736 (a) Section 753 also applies to payments under section 736 (a) made to the estate or other successor in interest of a deceased partner who, at the time of his death, was receiving payments as a retiring partner under section 736 (a) which payments are subsequently made to his estate or other successor in interest. (See § 1.706–1 (c) (3) for income with respect to a decedent partner included in the distributive share of such partner's estate or other successor in interest.)

(b) *Effective date.* The provisions of section 753 apply only in the case of payments made with respect to decedents dying after December 31, 1954. See section 771 (b) (4) and § 1.771 (b) (4)

§ 1.754 *Statutory provisions; manner of electing optional adjustment to basis of partnership property.*

SEC. 754. *Manner of electing optional adjustment to basis of partnership property.* If a partnership files an election, in accordance with regulations prescribed by the Secretary or his delegate, the basis of partnership property shall be adjusted, in the case of a distribution of property, in the manner provided in section 734 and, in the case of a transfer of a partnership interest, in the manner provided in section 743. Such an election shall apply with respect to all distributions of property by the partnership and to all transfers of interests in the partnership during the taxable year with respect to which such election was filed and all subsequent taxable years. Such election may be revoked by the partnership, subject to such limitations as may be provided by regulations prescribed by the Secretary or his delegate.

§ 1.754–1 *Time and manner of making election to adjust basis of partnership property*—(a) *In general.* A partnership may adjust the basis of partnership property under sections 734 (b) and 743 (b) if it files an election in accordance with the rules set forth in paragraph (b) below. An election may not be filed to make the adjustments provided in either section 734 (b) or section 743 (b) alone, but such an election must apply to both sections. An election made under the provisions of this section shall apply with respect to all property distributions and transfers of partnership interests taking place in the partnership taxable year with respect to which the election is made and in all subsequent partnership taxable years unless the election is revoked pursuant to paragraph (c) below.

(b) *Method of making election.* An election to adjust the basis of partnership property under sections 734 (b) and 743 (b) shall be made in a written statement filed with the district director with whom the returns of the partnership are required to be filed. The statement shall (1) set forth the name and address of the partnership making the election, (2) be signed by any one of the partners, and (3) contain a declaration that the partnership elects to apply the provisions of section 734 and section 743. The election shall be filed with the partnership return for the first taxable year to which the election applies.

(c) *Revocation of election.* A partnership having an election in effect under this section may, with the approval of the Commissioner, revoke such election. A partnership which wishes to revoke such an election shall file with the district director for the district in which the partnership return is required to be filed an application setting forth the grounds on which the revocation is desired. The application shall be filed not later than 30 days after the close of the partnership taxable year with respect to which the revocation is intended to take effect and shall be signed by any one of the partners. Examples of situations which may be considered sufficient reason for approving an application for revocation include a change in the nature of the partnership business, a substantial increase in the assets of the

partnership, a change in the character of partnership assets, or an increased frequency of retirements or shifts of partnership interests, so that an increased administrative burden would result to the partnership from the election. However, no application for revocation of an election shall be approved when the purpose of the revocation is to avoid stepping down the basis of partnership assets upon a transfer or distribution.

§ 1.755 *Statutory provisions; rules for allocation of basis.*

SEC. 755. *Rules for allocation of basis*—(a) *General rule.* Any increase or decrease in the adjusted basis of partnership property under section 734 (b) (relating to the optional adjustment to the basis of undistributed partnership property) or section 743 (b) (relating to the optional adjustment to the basis of partnership property in the case of a transfer of an interest in a partnership) shall, except as provided in subsection (b), be allocated—

(1) In a manner which has the effect of reducing the difference between the fair market value and the adjusted basis of partnership properties, or

(2) In any other manner permitted by regulations prescribed by the Secretary or his delegate.

(b) *Special rule.* In applying the allocation rules provided in subsection (a), increases or decreases in the adjusted basis of partnership property arising from a distribution of, or a transfer of an interest attributable to, property consisting of—

(1) Capital assets and property described in section 1231 (b), or

(2) Any other property of the partnership,

shall be allocated to partnership property of a like character except that the basis of any such partnership property shall not be reduced below zero. If, in the case of a distribution, the adjustment to basis of property described in paragraph (1) or (2) is prevented by the absence of such property or by insufficient adjusted basis for such property, such adjustment shall be applied to subsequently acquired property of a like character in accordance with regulations prescribed by the Secretary or his delegate.

§ 1.755–1 *Rules for allocation of basis*—(a) *General rule.* (1) (i) Where a partnership has filed an election under section 754 and § 1.754–1 to make the optional adjustments to basis of partnership property under the provisions of section 734 (b) (relating to the optional adjustment to the basis of undistributed partnership property) and section 743 (b) (relating to the optional adjustment to the basis of partnership property where a partnership interest is transferred) any increase or decrease in the adjusted basis of the partnership property shall, except as provided in paragraph (b) of this section, be allocated to the basis of the properties of the partnership (other than money) in a manner which will reduce the difference between the fair market value and the adjusted basis of partnership properties or shall be allocated in any other manner approved by the Commissioner under subparagraph (2)

(ii) If there is an increase in basis to be allocated to partnership assets, the entire adjustment must be allocated only to assets whose values exceed their bases and in proportion to the difference between the value and basis of each. However, no adjustment shall be made to any asset the adjusted basis of which equals or exceeds its fair market value.

(iii) If there is a decrease in basis to be allocated to partnership assets, the entire adjustment must be allocated to assets whose basis exceed their values and in proportion to the difference between the basis and value of each. However, no adjustment shall be made to any asset, the fair market value of which equals or exceeds its adjusted basis.

(iv) The application of the rule with respect to the allocation of an increase in basis under subdivision (ii) above requires that a portion of such adjustment be allocated to partnership good will, to the extent that such good will exists, in accordance with the excess of the value of such good will over its adjusted basis at the time of the transaction.

(2) If the partnership proposes to adjust the basis of its assets under section 734 (b) or 743 (b) in any other manner than that prescribed in subparagraph (1) an application for permission to use such other method must be filed with the district director not later than the time prescribed by law for the filing of the partnership return for the taxable year in which the proposed adjustment is to be made. The application must describe the proposed adjustments in detail and set forth the reasons for the desired use of the other method.

(b) *Special rules.* (1) Where there is a distribution of partnership property resulting under section 734 (b) in an adjustment to the basis of undistributed partnership property, such adjustment must be allocated to remaining partnership property of a character similar to that of the distributed property with respect to which the adjustment arose. For the purpose of applying this rule, the partnership property shall be classified into two categories: (i) capital assets and property described in section 1231 (b) (certain property used in the trade or business), or (ii) any other property of the partnership. Thus, when the adjusted basis in the hands of the partnership immediately prior to distribution of distributed capital assets and property described in section 1231 (b) exceeds the basis of such property to the distributee partner, as determined under section 732, the basis of the undistributed capital assets and property described in section 1231 (b) remaining in the partnership shall be increased by an amount equal to such excess. Conversely, when the basis to the distributee partner, as determined under section 732, of distributed capital assets and property described in section 1231 (b) exceeds the adjusted basis of such property in the hands of the partnership immediately prior to the distribution, the basis of the undistributed capital assets and property described in section 1231 (b) remaining in the partnership shall be decreased by an amount equal to such excess. Similarly, where there is a distribution of partnership property other than capital assets and property described in section 1231 (b) and the basis of such property to the distributee partner, as determined under section 732, is not the same as the adjusted basis of such property in the hands of the partnership immediately prior to distribution, the adjustment shall be made only to undistributed property of the same category remaining in the partnership.

(2) Where there is a basis adjustment under section 743 (b) arising from a transfer of an interest in a partnership by sale or exchange or upon the death of a partner, the amount of the adjustment shall be allocated to the same category of property (see subparagraph (1) above) as that with respect to which the basis adjustment arose. Thus, to the extent that an amount paid by a purchaser of a partnership interest (or the basis of the partnership interest to the estate or other successor in interest of a deceased partner) is attributable to the value of capital assets and property described in section 1231 (b), any difference between the amount so attributable and the transferee partner's proportionate share of the partnership basis of such property shall constitute a special basis adjustment with respect to partnership capital assets and property described in section 1231 (b), which is to be allocated in accordance with the rules stated in this section. Similarly, any such difference attributable to any other property of the partnership shall constitute a special basis adjustment with respect to such property and is to be allocated to such other property in accordance with the rules stated in this section.

(3) Where a decrease in the basis of partnership assets is required and the amount of the decrease exceeds the adjusted basis to the partnership of property of the required character, the basis of such property shall be reduced to zero (but not below zero) and the balance of the decrease in basis shall be made when the partnership subsequently acquires property of a like character to which an adjustment can be made.

(4) Where, in the case of a distribution, an increase or decrease required under paragraph (a) in the basis of undistributed partnership property cannot be made because the partnership owns no property of the character required to be adjusted, or because of insufficient adjusted basis for such property, the adjustment shall be made when the partnership subsequently acquires property of a like character to which an adjustment can be made.

(c) *Examples.* The provisions of this section may be illustrated by the following examples:

Example (1). Assume that partnership ABC has three assets: X, a capital asset with an adjusted basis of $1,000 and a fair market value of $1,500; Y, a depreciable asset with an adjusted basis of $1,000 and a value of $900; and Z, inventory items with an adjusted basis of $700 and a value of $600. A sells his interest to D (when an election under 754 is in effect) for $1,000 (⅓ of $3,000, the total fair market value of partnership assets). D's proportionate share of the adjusted basis of partnership property is $900 (⅓ of $2,700). Therefore, D has a special basis adjustment of $100 ($1,000 minus $900). This adjustment is to be allocated entirely to property X, since such allocation has the effect of reducing the difference between the value and basis of such asset. Therefore, D has a special basis adjustment of $100 with respect to property X, which now has a special basis to him of $1,100. No part of the adjustment is made to depreciable prop-

erty Y or inventory items Z, since any such adjustment would increase the difference between the basis and value of each such asset.

Example (2). Assume the same facts as in example (1) except that capital asset X has a fair market value of $1,500, depreciable property Y has a fair market value of $1,100, and inventory items Z have a fair market value of only $400. Therefore, D has a special basis adjustment of $100, the excess of D's basis for his interest in the partnership ($1,000) over his proportionate share of the adjusted basis of partnership property ($900). This $100 adjustment is allocated entirely to capital asset X and depreciable property Y in proportion to the difference between the value and basis of each, since such allocation has the effect of reducing the difference between the value and basis of each such asset. Therefore, D has a special basis adjustment of $83 ($500/$600 of $100) with respect to capital asset X, which now has a special basis to him of $1,083, and of $17 ($100/$600 of $100) with respect to depreciable property Y, which now has a special basis to him of $1,017. No part of the adjustment is made to inventory items Z, since any such adjustment would increase the difference between the basis of such asset and its value.

DEFINITIONS

§ 1.761 *Statutory provisions; terms defined.*

SEC. 761. *Terms defined*—(a) *Partnership.* For purposes of this subtitle, the term "partnership" includes a syndicate, group, pool, joint venture, or other unincorporated organization through or by means of which any business, financial operation, or venture is carried on, and which is not, within the meaning of this title, a corporation or a trust or estate. Under regulations the Secretary or his delegate may, at the election of all the members of an unincorporated organization, exclude such organization from the application of all or part of this subchapter, if it is availed of—

(1) For investment purposes only and not for the active conduct of a business, or

(2) For the joint production, extraction, or use of property, but not for the purpose of selling services or property produced or extracted,

if the income of the members of the organization may be adequately determined without the computation of partnership taxable income.

(b) *Partner.* For purposes of this subtitle, the term "partner" means a member of a partnership.

(c) *Partnership agreement.* For purposes of this subchapter, a partnership agreement includes any modifications of the partnership agreement made prior to, or at, the time prescribed by law for the filing of the partnership return for the taxable year (not including extensions) which are agreed to by all the partners, or which are adopted in such other manner as may be provided by the partnership agreement.

(d) *Liquidation of a partner's interest.* For purposes of this subchapter, the term "liquidation of a partner's interest" means the termination of a partner's entire interest in a partnership by means of a distribution, or a series of distributions, to the partner by the partnership.

§ 1.761–1 *Terms defined*—(a) *Partnership.* The term "partnership" includes a syndicate, group, pool, joint venture, or other unincorporated organization through or by means of which any business, financial operation, or venture is carried on, and which is not a corporation or a trust or estate within the meaning of the Internal Revenue Code of 1954. The term "partnership" is broader in scope than the common law meaning of partnership, and may include groups not commonly called partnerships. See section 7701 (a) (2).

(b) *Exclusion of certain partnerships from provisions of subchapter K*—(1) *In general.* Under the conditions set forth in this paragraph, an unincorporated organization may be excluded from the application of all or a part of the provisions of subchapter K. Such organization must be availed of (i) for investment purposes only and not for the active conduct of a business, or (ii) for the joint production, extraction, or use of property, but not for the purpose of selling services or property produced or extracted. The members of such organization must be able to compute their income without the necessity of computing partnership taxable income. Any syndicate, group, pool, or joint venture with centralized control or management which is classifiable as an association or any group operating under an agreement which creates an organization classifiable as an association does not fall within these provisions.

(2) *Investing partnership.* (i) Where the joint purchase, retention, sale, or exchange of investment property is undertaken in accordance with an agreement entered into after December 31, 1954, and the participants therein—

(*a*) Retain ownership thereof as co-owners whether in fee or under other form of contract, and

(*b*) As co-owners each reserves the right individually to take or dispose of his share of any property acquired or retained, and

(*c*) By such agreement do not propose the active conduct of business for joint profit, nor irrevocably authorize some person or persons acting in a representative capacity to purchase, sell, or exchange such investment property, although each separate participant may delegate authority to purchase, sell, or exchange his share of any such investment property for the time being for his account but not for a period of more than a year, then

such group is considered to be a partnership which may avail itself of the election to be excluded from the application of all or part of the provisions of subchapter K. This election may not be made unless each participant in the agreement may adequately determine his income with respect to his undivided interest without the computation of partnership taxable income. The election to be excluded, specifying those provisions of subchapter K from which exclusion is desired, must be included as part of the agreement, and a copy of such agreement must be attached to the first partnership return required to be filed by such organization. Such exclusion shall be effective to the extent approved by the Commissioner.

(ii) A qualified partnership return on Form 1065 shall be filed in the district in which a numerical majority of the participants in such agreement reside. Such return shall be filed for the first taxable year in which any activity occurs with respect to such agreement and for each taxable year thereafter. The return shall contain a statement showing the names and addresses of the co-owners, and the percentage of each co-owner's interest in the co-ownership, total costs and expenses billed each co-owner with respect to the purchase, custody, sale, or exchange of investment property, and the total revenue credited in any case where revenue was distributed to the co-owners (by way of credit or cash) from the sale or other disposition of any co-owner's share of investment property.

(3) *Mineral operating agreements.* (i) Where the joint production, extraction, or use of property is undertaken in accordance with the provisions of a joint operating agreement entered into after December 31, 1955, and the participants therein—

(*a*) Retain ownership thereof as co-owners whether in fee or under a lease or other form of contract granting exclusive operating rights, and

(*b*) As co-owners each reserves the right to take his share of any property produced in kind, and

(*c*) By such agreement do not provide for engaging in cycling, manufacturing, or processing operations for persons not members of such operating agreement and do not provide for the selling of services or property produced or extracted, although each separate participant may delegate authority to sell his share of minerals produced or extracted for the time being for his account but not for a period of time in excess of the minimum needs of the industry and in no event for more than one year, then

such group, if not taxable as a corporation or trust, is considered to be a partnership which may avail itself of the election to be excluded from the application of all or part of the provisions of subchapter K. This election may not be made unless each participant in the operating agreement may adequately determine his income with respect to his undivided interest without the computation of partnership taxable income. The election to be excluded, specifying those provisions of subchapter K from which exclusion is desired, must be included as part of the operating agreement, and a copy of such agreement must be attached to the first partnership return required to be filed by such organization. Such exclusion shall be effective to the extent approved by the Commissioner.

(ii) Where working interests in natural resources deposits are operated under an agreement entered into prior to January 1, 1956, and the participants—

(*a*) Retain ownership thereof as co-owners whether in fee or under a lease or other form of contract granting exclusive operating rights, and

(*b*) As co-owners each reserves the right to take his share of the product in kind, though he delegates authority to sell his share of production for the time being for his account, but not for a period of time in excess of the minimum needs of the industry and in no event for more than one year, then

for purposes of subtitle A such participants shall be considered as agreeing to separate accounting as individuals, and

the election under section 761 (a) with respect to the exclusion of partnerships from the application of all or part of subchapter K is not available unless the operating agreement is revised so that the value of minerals produced is established and accounted for as gross income of the partnership.

(iii) In the case of any joint operating agreement referred to in this subparagraph, a qualified partnership return on Form 1065 shall be filed by the operating co-owner under the operating co-owner's name for the first taxable year in which any activity occurs under the operating agreement, and for each taxable year thereafter. This qualified partnership return shall show the following information: a schedule showing the total working interest, names and addresses of the co-owners, the percentage of each co-owner's interest in the co-ownership, total costs and expenses billed each co-owner with respect to drilling for and producing the mineral, and the total revenue credited in those cases where the operating co-owner distributed revenue to the other co-owners (by way of credit or cash) from the sale or other disposition of such co-owners' share of production.

(c) *Partner* The term "partner" means member of a partnership.

(d) *Partnership agreement.* For the purposes of subchapter K, a partnership agreement will be considered to include any oral or written modification of the original agreement if such modification has been agreed to by all the partners or adopted in any other manner provided by the partnership agreement. A partnership agreement may be modified with respect to a particular taxable year subsequent to the close of such taxable year, but not later than the date (not including any extension of time) prescribed by law for the filing of the partnership return.

(e) *Liquidation of partner's interest.* The term "liquidation of a partner's interest" means the termination of a partner's entire interest in a partnership by means of a distribution, or a series of distributions, to the partner by the partnership. A series of distributions will come within the meaning of this term whether they are made in one year or in more than one year. Where a partner's interest is to be liquidated by a series of distributions, the interest will not be considered as liquidated until the final distribution has been made. For the basis of property distributed in one liquidating distribution, or in a series of distributions in liquidation, see section 732 (b) and § 1.732–1 (b).

EFFECTIVE DATE FOR SUBCHAPTER

§ 1.771 *Statutory provisions, effective date.*

SEC. 771. *Effective date*—(a) *General rule*—(1) *Taxable years beginning after December 31, 1954.* Except as provided in subsection (b), this subchapter shall apply with respect to—

(A) Any partnership taxable year beginning after December 31, 1954, and

(B) Any part of a partner's taxable year falling within such partnership taxable year.

(2) *Application of prior provisions.* Except as provided in subsection (b), sections 113 (a) (13), 181 to 191 (inclusive), and 3797 (a) (2) of the Internal Revenue Code of 1939 shall apply with respect to—

(A) Any partnership taxable year beginning before January 1, 1955, and

(B) Any part of a partner's taxable year falling within such partnership taxable year.

(b) *Special rules*—(1) *Adoption of taxable year.* Section 706 (b) (relating to the adoption of a taxable year by a partnership or partner) shall apply to—

(A) Any partnership which adopts, or changes to, a taxable year beginning after April 1, 1954, and

(B) Any partner who changes to a taxable year beginning after April 1, 1954.

For the purpose of applying this paragraph, section 708 (relating to the continuation of a partnership) shall be effective for taxable years beginning after April 1, 1954.

(2) *Property distributed by a partnership.* Section 735 (a) (relating to the character of gain or loss on the disposition of property distributed by a partnership) shall apply only to property distributed by a partnership after March 9, 1954.

(3) *Unrealized receivables and inventory items.* Section 751 (relating to unrealized receivables and inventory items) shall apply with respect to gain or loss to a seller, distributee, or partnership in the case of a sale, exchange, or distribution occurring after March 9, 1954. For the purpose of applying this paragraph in the case of a taxable year beginning before January 1, 1955, the other sections of this subchapter shall be applicable to the extent provided by regulations prescribed by the Secretary or his delegate.

(4) *Partner receiving income in respect of decedent.* Section 753 (relating to income in respect of a decedent) shall apply only in the case of payments made with respect to decedents dying after December 31, 1954.

(c) *Optional treatment of certain distributions.* In the case of a partnership taxable year beginning after December 31, 1953, and before January 1, 1955, a partnership may elect, under regulations prescribed by the Secretary or his delegate, with respect to distributions made during such year to any partner, other than in liquidation of the partner's interest, to apply the rules in sections 731, 732 (a), (c), and (e), 733, 735, and 751 (b), (c), and (d) (and, to the extent applicable, the rules provided in sections 705, 752, and 761 (d)). If a partnership so elects, such rules shall be effective for the partnership and all members of such partnership with respect to such distributions.

§ 1.771–1 *Effective date*—(a) *General rule.* Except as provided in paragraph (b) or (c) of this section, the provisions of subchapter K shall apply to any taxable year of a partnership beginning after December 31, 1954, and to any part of a partner's taxable year falling within such partnership taxable year. The provisions of the Internal Revenue Code of 1939 relating to partnerships shall apply to any taxable year of a partnership beginning before January 1, 1955, and to any part of a partner's taxable year falling within such partnership taxable year. If a partnership and the partners are on different taxable years, subchapter K shall become effective at the same time both for the partnership and for the partners.

(b) *Special rules.* Certain provisions of section 771 apply after specific dates in 1954, as follows:

(1) *Adoption of taxable year* Section 706 (b) (relating to the adoption of taxable years by partners and partnerships), shall apply to any partnership which adopts or changes to, and any partner who changes to, a taxable year beginning on or after April 2, 1954. For the purpose of applying this subparagraph the rules of section 708 (relating to the continuation of partnerships) shall apply. For example, if two or more partnerships merge after April 1, 1954, and the new partnership uses the taxable year of the partnership of which it is deemed to be the successor under section 708 (b) (2) (A) it will not need prior approval to continue to use such taxable year even though such year may be different from the taxable years of the partners. Such a partnership is not "adopting" or "changing" its taxable year.

(2) *Property distributed by a partnership.* Section 735 (a) relating to the character of gain or loss on disposition of property distributed by a partnership to a partner, shall apply only to property distributed after March 9, 1954. Although a partnership whose taxable year begins before January 1, 1955, generally will be subject to the provisions of the Internal Revenue Code of 1939, any unrealized receivables or inventory item distributed by any such partnership after March 9, 1954, will be subject to the provisions of section 735 (a) and the gain or loss on the subsequent disposition of such property will be ordinary gain or loss rather than capital gain or loss. In the case of property distributed before March 10, 1954, section 735 (a) will not apply, even though the property is disposed of by the distributee partner after that date.

(3) *Unrealized receivables and inventory items.* Section 751 (providing for the realization of ordinary income on certain transfers or distributions of unrealized receivables or substantially appreciated inventory items) shall be applicable to any such transfer occurring after March 9, 1954. For the purpose of applying section 751 in the case of a taxable year beginning before January 1, 1955, a partnership or partner may elect to treat as applicable any other section of subchapter K. See § 1.751–1 (f)

(4) *Partner receiving income in respect of decedent.* Section 753, which provides that the amount includible in the gross income of a successor in interest of a deceased partner under section 736 (a) shall be considered income in respect of a decedent under section 691, shall apply only in the case of payments made with respect to decedents dying after December 31, 1954.

(c) *Optional treatment of certain distributions.* (1) For a partnership taxable year beginning after December 31, 1953, and before January 1, 1955, a partnership may elect to apply the rules of certain sections of subchapter K with respect to current distributions made by the partnership in such year. These sections are 731, 732 (a) (c) and (e) 733, 735, and 751 (b), (c) and (d) If an election is made, it shall apply to the partnership and all its members for all current distributions made by the partnership during the taxable year. Such distributions shall also be subject to the rules of sections 705 (relating to determination of basis of a partner's interest) 752 (relating to treatment of certain liabilities) and 761 (d) (relating to

the definition of liquidation of a partner's interest) to the extent that such sections apply to current distributions.

(2) An election under this paragraph shall be made by a statement filed with the partnership return for the taxable year to which such election applies, or filed within 90 days after the promulgation of the regulations under section 771, whichever date is later. The statement shall be signed by all members of the partnership and the election once made shall be binding on the partnership and on all of its members.

[F. R. Doc. 55-6574; Filed, Aug. 11, 1955; 8:48 a. m.]

DEPARTMENT OF LABOR

Wage and Hour Division

[29 CFR Parts 655, 657, 671, 673, 696, 698, 706]

VARIOUS INDUSTRIES IN PUERTO RICO

NOTICE OF PUBLIC HEARING

In conformity with sections 5 and 8 of the Fair Labor Standards Act of 1938, notice is hereby given to all interested persons that consecutive public hearings will be held beginning on August 29, 1955, at 10:00 a. m., in Room 412, New York Department Store Building, Stop 16½, Ponce de Leon Avenue, Santurce, Puerto Rico, for the purpose of hearing such witnesses and receiving such evidence as may be necessary or appropriate to enable Special Industry Committees Nos. 17-A, 17-B, 17-C, 17-D, and 17-E for Puerto Rico to perform their duties and functions under this Act.

Special Industry Committees Nos. 17-A, 17-B, 17-C, 17-D, and 17-E for Puerto Rico were created by Administrative Order No. 443, as amended by Administrative Order No. 445, published in the FEDERAL REGISTER on June 10, 1955, and June 28, 1955, respectively, and have conducted hearings in Puerto Rico pursuant to notice published in the June 30, 1955, issue of the FEDERAL REGISTER (20 F. R. 4657) These additional hearings are hereby noticed in view of the changed procedure contemplated by the Fair Labor Standards Amendments of 1955 which have been enacted by the Congress and which may be approved by the President.

In accordance with the provisions of the Fair Labor Standards Act of 1938 and the regulations promulgated thereunder, the Committees are charged with the duty of investigating conditions in the following industries in Puerto Rico, as defined in said Administrative Orders: Special Industry Committee No. 17-A—Silk, Rayon, and Nylon Underwear Division, and the Miscellaneous Division of the Needlework and Fabricated Textile Products Industry; Special Industry Committee No. 17-B—Alcoholic Beverage and Industrial Alcohol Industry; Special Industry Committee No. 17-C—Food and Related Products Industries; Special Industry Committee No. 17-D—Tobacco Industry; and Special Industry Committee No. 17-E—Telephone Division, the Radio and Television Broadcasting Division, and the Gas Utility Division of the Communications, Utilities, and Miscellaneous Transportation Industries. These Committees have conducted investigations, and have held public hearings. They have tentatively decided to recommend the following wage rates:

Committee	Industry	Recommendations	Present rate
17-A	Needlework and Fabricated Textile Products:		
	Silk, Rayon, and Nylon Underwear Division:	*Cents*	*Cents*
	Hand-sewing operations	26	21
	Other operations	48	31
	General Division	46	46, 21, 30
17-B	Alcoholic Beverage and Industrial Alcohol Industry:		
	Malt Beverage Division	75	42½, 53
	General Division	75	60
17-C	Food and Related Products Industry:		
	Citron Brining Division	40	30
	General Division	46	30, 35, 42½
17-D	Tobacco Industry:		
	Filler Tobacco Processing Division (except machine chopping and related operations)	38	31
	General Division	60	31, 35, 36
17-E	Communications, Utilities, and Miscellaneous Transportation Industries:		
	Gas Utility Division	75	65
	Radio Broadcasting Division	65	55
	Telephone Division	75	70
	Television Broadcasting Division	75	65

These proceedings have been held pursuant to a notice and statute which contemplate that a further public hearing will be held to determine whether the minimum wage recommendations of the Committees should be approved or disapproved. If and when the Fair Labor Standards Amendments of 1955 become law, this procedure will be changed so the Secretary of Labor, without further hearing, will give effect to Industry Committee recommendations. The purpose of the hearings hereby noticed is to adapt the proceedings heretofore held to the requirements of the new enactment. Though the question whether the Amendments will become law will be settled prior to August 29, 1955, notice is issued at this time to give interested parties a greater opportunity to prepare. If the amendments do not become law, a notice will be issued cancelling these further hearings.

At the hearings hereby scheduled each committee will take official notice of the investigations, the testimony and other evidence theretofore received and considered by it. Transcripts of the public hearings of Committees Nos. 17-A and 17-B and the exhibits introduced at all the hearings are presently available for inspection, and transcripts of the public hearings of Committees Nos. 17-C, 17-D, and 17-E will be made available for inspection as soon as possible before August 29, 1955 at the Office of the Administrator of the Wage and Hour Division, United States Department of Labor, Washington 25, D. C., and at the office of the Territorial Director of the Wage and Hour Division, 412 New York Department Store Building, Stop 16½ Ponce de Leon Avenue, Santurce 29, Puerto Rico. A limited number of copies of the transcripts will also be available for distribution to interested parties on a showing of substantial need therefor.

Each Committee will, as a result of its public hearing hereby noticed, file with the Secretary of Labor a report containing its findings of fact and recommendations with respect to the matter referred to it. These findings of fact and recommendations will specify minimum wage rates for all employees in Puerto Rico in the industries mentioned above who are "engaged in commerce or in the production of goods for commerce", within the meaning of said Act, and who are entitled to its minimum wage benefits. These will be the highest rates, not in excess of 75 cents per hour, which, having due regard to economic and competitive conditions, will not substantially curtail employment in such industries and will not give any industry in Puerto Rico a competitive advantage over any industry in the United States outside of Puerto Rico.

Any person who, in the opinion of a Committee, or its duly authorized subcommittee, has a substantial interest in the proceeding and is prepared to present evidence pertinent to the questions under consideration will be afforded an opportunity to be heard. Each person who desires to participate in the hearings hereby noticed must file a notice of appearance, and may file written statements or briefs for the consideration of the Committees not later than August 26, 1955. The notice published in the FEDERAL REGISTER on June 4, 1955, contains illustrations of the types of information which the Committees are interested in receiving. Eight copies of such statements or briefs should be filed with the office of the Territorial Director of the Wage and Hour Division, Post Office Box 9061, Santurce 29, Puerto Rico. Written statements or briefs containing factual data submitted by persons who cannot appear personally will be considered by the Committees provided that such statements or briefs are sworn.

With the approval of a majority of all members of each of the Committees, and pursuant to 29 CFR 511.11, Jaime Benitez, Chairman of Special Industry Committees Nos. 17-A, 17-B, 17-C, 17-D, and 17-E, has requested the Office of the Administrator to insert in the FEDERAL REGISTER and to make public by a general press release this notice of the time, place, and scope of such hearings.

Signed at Washington, D. C., this 9th day of August 1955.

STUART ROTHMAN,
Solicitor of Labor

[F. R. Doc. 55-6586; Filed, Aug. 11, 1955; 8:50 a. m.]

NOTICES

DEPARTMENT OF THE INTERIOR

Bureau of Land Management

NEVADA

NOTICE OF PROPOSED WITHDRAWAL AND RESERVATION OF LANDS

The Department of the Navy, District Public Works Office, 12th Naval District, San Bruno, California, has filed an application, Serial No. Nevada 040230, for the withdrawal of the lands described below, from all forms of appropriation and use including grazing, mineral leasing and mining locations. The applicant desires the land for training aircraft in air to air gunnery.

For a period of 30 days from the date of publication of this notice, persons having cause may present their objections in writing to the undersigned official of the Bureau of Land Management, Department of the Interior, at P O. Box 1551, Reno, Nevada.

If circumstances warrant it, a public hearing will be held at a convenient time and place, which will be announced.

The determination of the Secretary on the application will be published in the FEDERAL REGISTER. A separate notice will be sent to each interested party of record.

The lands involved in the application are:

Beginning at the corner of Secs. 13, 18, 19 and 24 of Ts. 33 N., Rs. 23 and 24 E., thence westerly 6 miles more or less along the line between Secs. 13 and 24, 14 and 23, 15 and 22, 16 and 21, 17 and 20, 18 and 19 to the corner of Secs. 18 and 19 on the west boundary of T. 33 N., R. 23 E.

Thence northerly 9 miles more or less along the line between Ts. 33 and 34 N., Rs. 22 and 23 E., to the corner of Ts. 34 and 35 N., Rs. 22 and 23 E.

Thence westerly 6 miles more or less between Ts. 34 and 35 N., R. 22 E., to the closing corner of Ts. 34 and 35 N., R. 22 E., on the east boundary of T. 35 N., R. 21 E.

Thence northerly 6 miles more or less along the line between Ts. 35 N., Rs. 21 and 22 E., to the closing corner of Ts. 35 N., Rs. 21 and 22 E., on the 7th Standard Parallel North.

Thence westerly 4 miles more or less, along the 7th Standard Parallel north to the standard corner of Secs. 33 and 34, T. 36 N., R. 21 E.

Thence northerly 6 miles more or less along the line between Secs. 33 and 34, 27 and 28, 21 and 22, 15 and 16, 9 and 10, 3 and 4, to the corner of Secs. 3, 4, 33 and 34, Ts. 36 and 37 N., R. 21 E.

Thence westerly 3 miles more or less along the line between Ts. 36 and 37 N., R. 21 E., to the corner of Ts. 36 and 37 N., Rs. 20 and 21 E.

Thence northerly 6 miles more or less along the line between Ts. 37 N., Rs. 20 and 21 E., to the corner of Ts. 37 and 38 N., Rs. 20 and 21 E.

Thence westerly 6 miles more or less along the line between Ts. 37 and 38 N., R. 20 E., to the corner of Ts. 37 and 38 N., R. 20 E., on the east boundary of T. 37 N., R. 19 E.

Thence northerly 6 miles more or less along the line between Rs. 19 and 20 E., to the corner of Ts. 38 and 39 N., R. 19 E., on the west boundary of T. 39 N., R. 20 E.

Thence westerly 6 miles more or less along the line between Ts. 38 and 39 N., R. 19 E., to the corner of Ts. 38 and 39 N., Rs. 18 and 19 E.

Thence northerly 8½ miles more or less along the line between Ts. 39 N., Rs. 18 and 19 E., to the closing corner of Ts. 39 N., Rs. 18 and 19 E., on the south boundary of T. 40 N., R. 18 E.

Thence easterly 7 miles more or less along the south boundary of Ts. 40 N., Rs. 18 and 19 E., to the corner of Ts. 40 N., Rs. 19 and 20 E.

Thence northerly 6 miles more or less along the line between Ts. 40 N., Rs. 19 and 20 E., to the corner of Ts. 40 N., Rs. 19 and 20 E., on the south boundary of T. 41 N., R. 20 E.

Thence easterly 5½ miles more or less along the 8th Standard Parallel north to the standard corner of Ts. 41 N., Rs. 20 and 21 E.

Thence northerly 6 miles more or less along the line between Ts. 41 N., Rs. 20 and 21 E. to the corner of Ts. 41 and 42 N., Rs. 20 and 21 E.

Thence easterly 6 miles more or less along the line between Ts. 41 and 42 N., R. 21 E. to the corner of Ts. 41 and 42 N., Rs. 21 and 22 E.

Thence northerly 3 miles more or less along the line between Ts. 42 N., Rs. 21 and 22 E., to the corner of Secs. 13, 18, 19 and 24, Ts. 42 N., Rs. 21 and 22 E.

Thence easterly 6 miles more or less along the line between Secs. 18 and 19, 17 and 20, 16 and 21, 15 and 22, 14 and 23, 13 and 24, to the corner of Secs. 13, 18, 19, and 24, Ts. 42 N., Rs. 22 and 23 E.

Thence northerly 3 miles more or less between Ts. 42 N., Rs. 22 and 23 E., to the corner of Ts. 42 and 43 N., Rs. 22 and 23 E.

Thence easterly 6 miles more or less along the line between Ts. 42 and 43 N., R. 23 E., to the SE corner of T. 43 N., R. 23 E.

Thence southerly 11.16 chains more or less to the SW corner of T. 43 N., R. 24 E.

Thence easterly 7½ miles more or less along the south boundary of Ts. 43 N., Rs. 24 and 24½ E., to the corner of Ts. 42 and 43 N., R. 24½ E., on the west boundary of T. 42 N., R. 25 E.

Thence northerly 12.67 chains more or less to the corner of Ts. 42 and 43 N., R. 25 E., on the east boundary of T. 43 N., R. 24½ E.

Thence easterly 6 miles more or less along the line between Ts. 42 and 43 N., R. 25 E. to the corner of Ts. 42 and 43 N., R. 25 E. on the west boundary of T. 42 N., R. 26 E.

Thence northerly 1.13 chains more or less along the line between Rs. 25 and 26 E., to the corner of Ts. 42 and 43 N., R. 26 E. on the east boundary of T. 43 N., R. 25 E.

Thence easterly 6 miles more or less along the line between Ts. 42 and 43 N., R. 26 E., to the SE corner of T. 43 N., R. 26 E.

Thence northerly 6.72 chains more or less to the SW corner of T. 43 N., R. 27 E., on the east boundary of T. 43 N., R. 26 E.

Thence easterly 6 miles more or less along the line between Ts. 42 and 43 N., R. 27 E., to the corner of Ts. 42 and 43 N., R. 27 E., on the west boundary of T. 42 N., R. 28 E.

Thence northerly 18.54 chains more or less along the line between Rs. 27 and 28 E., to the closing corner of Ts. 42 and 43 N., R. 28 E.

Thence easterly 6 miles more or less along the line between Ts. 42 and 43 N., R. 28 E., to the corner of Ts. 42 and 43 N., Rs. 28 and 29 E.

Thence easterly 1 mile more or less to the corner of Secs. 5, 6, 31 and 32, Ts. 42 and 43 N., R. 29 E.

Thence east 1 mile more or less to a point north of the SW corner of T. 41 N., R. 30 E.

Thence south 12 miles more or less to a point east of the standard corner of Ts. 41 N., Rs. 28 and 29 E.

Thence west 2 miles more or less to the standard corner of Ts. 41 N., Rs. 28 and 29 E.

Thence westerly 3 miles more or less along the 8th Standard Parallel north to the standard corner of Secs. 33 and 34, T. 41 N., R. 28 E.

Thence south 6 miles more or less to a point east of the corner of Ts. 39 and 40 N., Rs. 27 and 28 E.

Thence west 3 miles more or less to the corner of Ts. 39 and 40 N., Rs. 27 and 28 E.

Thence south 6 miles.

Thence west 3 miles.

Thence south 12 miles more or less to a point east of the corner of Ts. 36 and 37 N., Rs. 26 and 27 E.

Thence west 3 miles more or less to the corner of Ts. 36 and 37 N., Rs. 26 and 27 E.

Thence southerly 6½ miles more or less along the line between Ts. 36 N., Rs. 26 and 27 E., to the standard corner of Ts. 36 N., Rs. 26 and 27 E.

Thence westerly 12½ miles more or less along the 7th Standard Parallel north through Rs. 26, 25, and a portion of 24, E., to the closing corner of Ts. 35 N., Rs. 24 and 25 E.

Thence southerly 6½ miles more or less along the line between Ts. 35 N., Rs. 24 and 25 E., to the corner of Ts. 34 and 35 N., Rs. 24 and 25 E.

Thence south 6 miles more or less to a point east of the corner of Secs. 3, 4, 33, and 34, Ts. 33 and 34 N., R. 24 E.

Thence west 3 miles more or less to the corner of Secs. 3, 4, 33 and 34, Ts. 33 and 34 N., R. 24 E.

Thence south 3 miles more or less to a point east of the corner of Secs. 13, 18, 19 and 24, Ts. 33 N., Rs. 23 and 24 E.

Thence west 3 miles more or less to the corner of Secs. 13, 18, 19, and 24, Ts. 33 N., Rs. 23 and 24 E., to the point of beginning.

Inclosing an area of approximately 1,372,160 acres.

Also beginning at the corner of Secs. 15, 16, 21 and 22, T. 25 N., R. 28 E., M. D. M., Nevada, thence northerly 3 miles more or less along the line between Secs. 15 and 16, 9 and 10, 3 and 4, to the closing corner of Secs. 3 and 4 on the 5th Standard Parallel north.

Thence westerly 3.26 chains more or less along the 5th Standard Parallel north to the standard corner of Secs. 33 and 34, T. 26 N., R. 28 E.

Thence northerly 6 miles more or less along the line between Secs. 33 and 34, 27 and 28, 21 and 22, 15 and 16, 9 and 10, 3 and 4, to the closing corner of Secs. 3 and 4, T. 26 N., R. 28 E.

Thence westerly 8.21 chains more or less along the south boundary of T. 27 N., R. 28 E., to the corner of Secs. 33 and 34, T. 27 N., R. 28 E.

Thence northerly 6 miles more or less along the line between Secs. 33 and 34, 27 and 28, 21 and 22, 15 and 16, 9 and 10, 3 and 4, to the closing corner of Secs. 3 and 4, T. 27 N., R. 28 E.

Thence easterly 3.03 chains more or less along the south boundary of T. 28 N., R. 28 E., to the corner of Secs. 33 and 34, T. 28 N., R. 28 E.

Thence northerly 6 miles more or less along the line between Secs. 33 and 34, 27 and 28, 21 and 22, 15 and 16, 9 and 10, 3 and 4, to the closing corner of Secs. 3 and 4, T. 28 N., R. 28 E.

Thence westerly 1.12 chains more or less along the south boundary of T. 29 N., R. 28 E., to the corner of Secs. 33 and 34, T. 29 N., R. 28 E.

Thence northerly 12 miles more or less along the line between Secs. 33 and 34, 27 and 28, 21 and 22, 15 and 16, 9 and 10, 3 and 4, of T. 29 N., R. 28 E., and Secs. 33 and 34, 27 and 28, 21 and 22, 15 and 16, 9 and 10, 3 and 4, of T. 30 N., R. 28 E., to the closing corner of Secs. 3 and 4, T. 30 N., R. 28 E.

Thence easterly 0.56 chains more or less along the 6th Standard Parallel north to the standard corner of Secs. 33 and 34, T. 31 N., R. 28 E.

Thence northerly 6 miles more or less on a straight line through unsurveyed T. 31 N., R. 28 E., to the corner of Secs. 3, 4, 33 and 34, Ts. 31 and 32 N., R. 28 E.

Thence northerly 6 miles more or less along the line between Secs. 33 and 34, 27 and 28, 21 and 22, 15 and 16, 9 and 10, 3 and 4, to the corner of Secs. 3 and 4, 33 and 34, Ts. 32 and 33 N., R. 28 E.

Thence westerly 3 miles more or less along the line between Ts. 32 and 33 N., R. 28 E., to the corner of Ts. 32 and 33 N., Rs. 27 and 28 E.

Thence west 6 miles.

Thence north 6 miles.

Thence east 9 miles.

Thence north 5 miles more or less to a point west of the corner of Secs. 1, 6, 7, and 12, Ts. 34 N., Rs. 30 and 31 E.

Thence east 15 miles more or less to the corner of Secs. 1, 6, 7 and 12, Ts. 34 N., Rs. 30 and 31 E.

Thence northerly 1½ miles more or less along the line between Ts. 34 N., Rs. 30 and 31 E., to the closing corner of Ts. 34 N., Rs. 30 and 31 E., on the south boundary of T. 35 N., R. 31 E.

Thence easterly 6 miles more or less along the line between Ts. 34 and 35 N., to the closing corner of T. 34 N., R. 31 E., on the south boundary of T. 35 N., R. 32 E.

Thence easterly 2 miles and 77.08 chains along the south boundary of T. 35 N., R. 32 E., as resurveyed in 1888.

Thence southerly 6½ miles more or less on a straight line to the corner of Secs. 3 and 4, on the north boundary of T. 33 N., R. 32 E.

Thence southerly 12 miles more or less along the line between Secs. 3 and 4, 9 and 10, 15 and 16, 21 and 22, 27 and 28, 33 and 34, T. 33 N., R. 32 E., and Secs. 3 and 4, 9 and 10, 15 and 16, 21 and 22, 27 and 28, 33 and 34, T. 32 N., R. 32 E., to the corner of Secs. 33 and 34, T. 32 N., R. 32 E.

Thence westerly 26.88 chains more or less along the south boundary of T. 32 N., R. 32 E., to the closing corner of Secs. 3 and 4, T. 31 N., R. 32 E.

Thence southerly 6 miles more or less along the line between Secs. 3 and 4, 9 and 10, 15 and 16, 21 and 22, 27 and 28, 33 and 34, to the standard corner of Secs. 33 and 34, T. 31 N., R. 32 E.

Thence westerly 3 miles more or less along the 6th Standard Parallel north to the closing corner of Ts. 30 N., Rs. 31 and 32 E.

Thence southerly 6 miles more or less along the line between Ts. 30 N., Rs. 31 and 32 E., to the corner of Ts. 29 and 30 N., Rs. 31 and 32 E.

Thence westerly 3 miles more or less to the corner of Secs. 3, 4, 33 and 34, Ts. 29 and 30 N., R. 31 E.

Thence southerly 6 miles more or less along the line between Secs. 3 and 4, 9 and 10, 15 and 16, 21 and 22, 27 and 28, 33 and 34, to the corner of Secs. 33 and 34, T. 29 N., R. 31 E.

Thence westerly 3 miles more or less along the line between Ts. 28 and 29 N., R. 31 E., to the closing corner of Ts. 28 and 29 N., R. 31 E., on the east boundary of T. 28 N., R. 30 E.

Thence southerly 5½ miles more or less along the line between Ts. 28 N., Rs. 30 and 31 E., to the corner of Ts. 27 and 28 N., R. 30 E.

Thence westerly 6 miles more or less along the line between Ts. 27 and 28 N., R. 30 E., to the corner of Ts. 27 and 28 N., Rs. 29 and 30 E.

Thence southerly 6 miles more or less along the line between Ts. 27 N., Rs. 29 and 30 E., to the corner of Ts. 26 and 27 N., Rs. 29 and 30 E.

Thence westerly 3 miles more or less along the line between Ts. 26 and 27 N., R. 29 E., to the corner of Secs. 3, 4, 33 and 34, Ts. 26 and 27 N., R. 29 E.

Thence southerly 6 miles more or less along the line between Secs. 3 and 4, 9 and 10, 15 and 16, 21 and 22, 27 and 28, 33 and 34, to the standard corner of Secs. 33 and 34, T. 26 N., R. 29 E., on the 5th Standard Parallel north.

Thence westerly 3 miles more or less along the 5th Standard Parallel north to the closing corner of Ts. 25 N., Rs. 28 and 29 E.

Thence southerly 3 miles more or less along the east boundary of T. 25 N., R. 28 E., to the corner of Secs. 13 and 24, T. 25 N., R. 28 E.

Thence westerly 3 miles more or less along the line between Secs. 13 and 24, 14 and 23, 15 and 22, to the corner of Secs. 15, 16, 21 and 22, T. 25 N., R. 28 E., the point of beginning.

Inclosing an area of approximately 654,720 acres.

Dated: August 4, 1955.

E. R. GREENSLET,
State Supervisor

[F. R. Doc. 55-6563; Filed, Aug. 11, 1955; 8:46 a. m.]

[Area Order 4]

COLORADO

MODIFICATION OF COLORADO GRAZING DISTRICTS NO. 2 AND 7

Correction

In Federal Register Document 55-5630, appearing at page 5023 in the issue for Thursday, July 14, 1955, the name of the Area Administrator should read "W B. Wallace"

Geological Survey

SNAKE RIVER BASIN, WYOMING

POWER SITE CLASSIFICATION NO. 433

Pursuant to authority vested in me by the act of March 3, 1879 (20 Stat. 394; 43 U. S. C. 31) and by Departmental Order No. 2333 of June 10, 1947 (43 CFR 4.623; 12 F. R. 4025) the following described land is hereby classified as power sites insofar as title thereto remains in the United States and subject to valid existing rights; and this classification shall have full force and effect under the provisions of section 24 of the act of June 10, 1920, as amended by section 211 of the act of August 26, 1935 (16 U. S. C. 818)

SIXTH PRINCIPAL MERIDIAN, WYOMING

T. 41 N., R. 111 W.,
Sec. 5, lots 3 and 4, S½NW¼, N½SW¼ and SE¼SW¼,
Sec. 6, lots 1, 2, 3, SE¼NE¼, SE¼NW¼ and E½SW¼.
Sec. 7, lots 1, 2, 3, 4, and E½W½,
Sec. 18, lots 1, 2, 3, and 4;
Sec. 19, lot 3, SW¼NE¼, E½NW¼, W½ SE¼ and SE¼SE¼,
Sec. 29, W½NW¼,
Sec. 30, lot 2, NE¼NE¼ and SE¼NW¼.

T. 42 N., R. 111 W.,
Sec. 28, W½NE¼, NE¼NW¼, S½NW¼, SW¼ and NW¼SE¼,
Sec. 29, S½SW¼, N½SE¼, N½SW¼SE¼ and SE¼SE¼,
Sec. 30, lot 4, SE¼SW¼ and SW¼SE¼,
Sec. 31, lots 1, 2, 3, 4, N½NE¼NE¼, SW¼ NE¼NE¼, W½NE¼, S½SE¼NE¼, NE¼NW¼, E½SW¼ and SE¼,
Sec. 32, NE¼NE¼, S½NW¼NE¼, SW¼ NE¼, NE¼SW¼NW¼, S½SW¼NW¼, SE¼NW¼ and N½SW¼,
Sec. 33, N½NW¼.

T. 41 N., R. 112 W.,
All unsurveyed lands adjacent to the Gros Ventre River at an altitude of less than 7,600 feet above sea level. Protraction of public land surveys indicates that the above-described lands when surveyed will be in sections 1, 2, 3, 11, 12, 13, 24 and 25.

T. 42 N., R. 112 W.,
Sec. 34, SE¼SE¼,
Sec. 35, NE¼NE¼, S½NE¼, and S½,
Sec. 36.

T. 45 N., R. 112 W.,
Unsurveyed island in secs. 20 and 21;
Sec. 13, S½SW¼,
Sec. 14, S½S½,
Sec. 15, S½SW¼, NE¼SE¼, and S½SE¼;
Sec. 19, lots 4, 5, and 6, and W½SE¼,
Sec. 20, lots 1 to 8, inclusive, NE¼NE¼, SW¼NE¼, and S½NW¼,
Sec. 21, lots 1, 4, 5, 6, 9, 10, 11, 12, 13, 14, and 15, NW¼NE¼, NE¼SW¼NE¼, N½ NW¼, and SE¼SE¼,
Sec. 22, lots 1 to 8, inclusive, and NW¼ SW¼,
Sec. 23, lots 1 to 8, inclusive, SE¼NE¼, and S½NW¼,
Sec. 24, lot 1, NW¼NE¼, and NE¼NW¼,
Sec. 28, NW¼NW¼,
Sec. 29, lots 1 and 2, NE¼, NE¼NW¼, S½ NW¼, N½SW¼, and SW¼SW¼,
Sec. 30;
Sec. 31, N½NE¼.

T. 37 N., R. 113 W.,
Sec. 3, lot 1;
Sec. 4, lots 1 and 2.

T. 38 N., R. 113 W.,
Sec. 16, W½NE¼, E½NW¼, NE¼SW¼, S½SW¼, NW¼SE¼, and S½SE¼,
Sec. 17, SW¼,
Sec. 18, lots 2 and 3, NE¼SW¼, N½SE¼ SW¼, and SE¼SE¼SW¼,
Sec. 19, lots 2 and 3, N½NE¼, SE¼NE¼, S½SE¼NW¼, E½SW¼, SW¼SE¼, and S½SE¼SE¼,
Sec. 20, SE¼NE¼, W½, and NW¼SE¼,
Sec. 21, SE¼,
Sec. 22, N½SW¼,
Sec. 28, N½NW¼, SW¼SW¼, NW¼SE¼, and SE¼SE¼,
Sec. 29, NW¼NE¼, NE¼NW¼, N½NW¼ NW¼, S½SW¼NW¼, N½SW¼, and E½SE¼,
Sec. 30, N½NE¼, SE¼NE¼, and NE¼ NW¼,
Sec. 32, NE¼NE¼,
Sec. 33, NE¼NE¼, W½NW¼, SE¼NW¼, and NW¼SW¼.

T. 38 N., R. 114 W.,
Sec. 13 (unsurveyed);
Sec. 23, NE¼ and N½NW¼,
Sec. 24, S½NE¼, W½NE¼NW¼, W½ NW¼, SE¼NW¼, and unsurveyed S½;
All unsurveyed lands adjacent to Hoback River at an altitude of less than 6,400 feet above sea level. Protraction of public land surveys, indicates that the above-described lands when surveyed will be in sections 4, 5, 6, 8, 9, 10, 14, 15, and 22.

T. 38 N., R. 115 W.,
Sec. 4, N½NE¼ and SE¼NE¼,
All lands in unsurveyed sections 1, 2, 3, 10, 11, and 12, at an altitude of less than 6,300 feet above sea level.

The area described aggregates about 18,283 acres.

Dated: August 5, 1955.

ARTHUR A. BAKER,
Acting Director

[F. R. Doc. 55-6560; Filed, Aug. 11, 1955; 8:45 a. m.]

CIVIL AERONAUTICS BOARD

[Docket No. 7218]

WEST COAST AIRLINES, INC.

NOTICE OF HEARING

In the matter of West Coast Airlines, Inc., permanent certification Show Cause Order, E-9426.

Notice is hereby given pursuant to the Civil Aeronautics Act of 1938, as amended, that a hearing in the above-entitled matter is assigned to be held on August 22, 1955, at 10:00 a. m., e. d. s. t., in Room 5855, Commerce Building, Fourteenth Street and Constitution Avenue NW., Washington, D. C., before Examiner Edward T. Stodola.

Dated at Washington, D. C., August 9, 1955.

[SEAL] FRANCIS W BROWN,
Chief Examiner.

[F. R. Doc. 55-6580; Filed, Aug. 11, 1955; 8:49 a. m.]

[Docket No. 7319]

WESTERN AIR LINES, INC., CASPER CUT-OFF RENEWAL CASE

NOTICE OF PREHEARING CONFERENCE

In the matter of the application of Western Air Lines, Inc., under section 401 of the Civil Aeronautics Act of 1938, as amended, for an order making permanent the amendment of its certificate of public convenience and necessity for Route 35, so as to extend said route beyond Rapid City, South Dakota, to the terminal point Salt Lake City, Utah, via the intermediate point Casper, Wyoming.

Notice is hereby given that a prehearing conference in the above-entitled proceeding is assigned to be held on September 23, 1955, at 10:00 a. m., e. d. s. t., in Room E-210, Temporary Building No. 5, Sixteenth Street and Constitution Avenue NW., Washington, D. C., before Examiner Edward T. Stodola.

Dated at Washington, D. C., August 9, 1955.

[SEAL] FRANCIS W. BROWN,
Chief Examiner

[F. R. Doc. 55-6581; Filed, Aug. 11, 1955; 8:49 a. m.]

[Docket No. 5701 et al.]

FLORIDA-TEXAS SERVICE CASE

NOTICE OF PREHEARING CONFERENCE

Notice is hereby given that a prehearing conference in the above-entitled proceeding is assigned to be held on September 7, 1955, at 10:00 a. m., e. d. s. t., in Room E-210, Temporary Building No. 5, Sixteenth Street and Constitution Avenue NW., Washington, D. C., before Examiner Ferdinand D. Moran.

Dated at Washington, D. C., August 8, 1955.

[SEAL] FRANCIS W BROWN,
Chief Examiner

[F. R. Doc. 55-6582; Filed, Aug. 11, 1955; 8:50 a. m.]

[Docket No. 7278]

LINEAS AEREAS DE NICARAGUA, S. A.

NOTICE OF PREHEARING CONFERENCE

In the matter of the application of Lineas Aereas de Nicaragua, S. A., for a foreign air carrier permit authorizing it to engage in indirect foreign air transportation with respect to property or as a foreign air freight forwarder between any point in the United States and any point in Nicaragua.

Notice is hereby given that a prehearing conference in the above-entitled proceeding is assigned to be held on September 8, 1955, at 10:00 a. m., e. d. s. t., in Room 2044, Temporary Building No. 5, Sixteenth Street and Constitution Avenue NW., Washington, D. C., before Examiner Joseph L. Fitzmaurice.

Dated at Washington, D. C., August 8, 1955.

[SEAL] FRANCIS W. BROWN,
Chief Examiner

[F. R. Doc. 55-6583; Filed, Aug. 11, 1955; 8:50 a. m.]

FARM CREDIT ADMINISTRATION

[Farm Credit Administration Order 631]

CHIEF OR ACTING CHIEF, AND ASSISTANT TO CHIEF, ADMINISTRATIVE DIVISION

AUTHORIZATION TO AUTHENTICATE DOCUMENTS, CERTIFY OFFICIAL RECORDS, AND AFFIX SEAL

V V Hemstreet, Chief, T. L. Piper, when Acting Chief, and Zelina A. Ahern, Assistant to the Chief, Administrative Division, severally and not jointly, are authorized and empowered:

(a) To execute and issue under the seal of the Farm Credit Administration, statements (1) authenticating copies of, or excerpts from, official records and files of the Farm Credit Administration; (2) certifying, on the basis of the records of the Farm Credit Administration, the effective periods of regulations, orders, instructions, and regulatory announcements; and (3) certifying, on the basis of the records of the Farm Credit Administration, the appointment, qualification, and continuance in office of any officer or employee of the Farm Credit Administration, or any conservator or receiver acting under the supervision or direction of the Farm Credit Administration.

(b) To sign official documents and to affix the seal of the Farm Credit Administration thereon for the purpose of attesting the signatures of officials of the Farm Credit Administration.

The foregoing revokes Farm Credit Administration Order No. 517, dated December 15, 1950, 15 F. R. 9194.

[SEAL] A. T. ESGATE,
Acting Governor.

[F. R. Doc. 55-6570; Filed, Aug. 11, 1955; 8:48 a. m.]

FEDERAL POWER COMMISSION

[Docket No. G-7341, etc.]

H. MERLYN CHRISTIE ET AL.

NOTICE OF FINDINGS AND ORDER

AUGUST 8, 1955.

In the matters of H. Merlyn Christie, et al., Docket No. G-7341, Robert A. Stacy, Docket No. G-7369; R. H. Abercrombie, Docket No. G-7370; C. M. Abercrombie, Docket No. G-7371, Goldston Oil Corporation, et al., Docket Nos. G-7372 and G-7373; Hiawatha Oil & Gas Company, Docket No. G-7375; Paul E. Barnhart, et al., Docket Nos. G-7378, G-7379; G-7380, G-7381, G-7382, G-7383, G-7384, G-7385, G-7386, G-7387, G-7388, and G-7389.

Notice is hereby given that on July 13, 1955, the Federal Power Commission issued its findings and order adopted July 13, 1955, issuing certificates of public convenience and necessity in the above-entitled matters.

[SEAL] J. H. GUTRIDE,
Acting Secretary.

[F. R. Doc. 55-6564; Filed, Aug. 11, 1955; 8:47 a. m.]

[Docket No. E-6639]

PUGET SOUND POWER & LIGHT CO.

NOTICE OF APPLICATION FOR DETERMINATION AS TO WHETHER APPLICANT IS A PUBLIC UTILITY

AUGUST 8, 1955.

Take notice that on August 3, 1955, an application was filed with the Federal Power Commission by Puget Sound Power & Light Company ("Applicant") for a determination whether or not Applicant is a "public utility" as defined in section 201 of the Federal Power Act, and if Applicant is determined to be a "public utility", for authorization of the issuance of securities under section 204 (a) of the Federal Power Act. Applicant is a corporation organized under the laws of the State of Massachusetts and doing business in the State of Washington, with its principal business office at Seattle, Washington. Applicant seeks authority to issue unsecured promissory notes in the aggregate amount of $20,000,000 to certain banks to evidence loans which it proposes to make during the period commencing August 1, 1955, and ending July 31, 1958. Said promissory notes will be issued subsequent to August 1, 1955, and will mature on July 31, 1958. The notes will bear interest at the rate of 3 percent per annum and Applicant will be obligated to pay a commitment fee on the first day of each January, April, July and October at the

rate of ¼ of 1 percent per annum based on the daily average of the unused remaining commitment. The proceeds from the issuance of said notes will be used to discharge certain bank loans now outstanding and to finance Applicant's construction program; all as more fully appears in the application on file with the Commission.

Any person desiring to be heard, or to make any protest with reference to said application should, on or before the 29th day of August 1955, file with the Federal Power Commission, Washington 25, D. C., a petition or protest in accordance with the Commission's Rules of Practice and Procedure. The application is on file with the Commission for public inspection.

[SEAL] J. H. GUTRIDE,
Acting Secretary.

[F. R. Doc. 55-6565; Filed, Aug. 11, 1955; 8:47 a. m.]

[Docket No. G-5205]

PHIL K. COCHRAN

NOTICE OF APPLICATION AND DATE OF HEARING

AUGUST 8, 1955.

Take notice that Phil K. Cochran, Applicant, an individual whose address is Commercial National Bank Building, Shreveport, Louisiana, filed on November 22, 1954, an application for a certificate of public convenience and necessity pursuant to section 7 of the Natural Gas Act, authorizing Applicant to render service as hereinafter described, subject to the jurisdiction of the Commission, all as more fully represented in the application which is on file with the Commission and open for public inspection.

Applicant proposes to sell natural gas in interstate commerce to the Arkansas Louisiana Gas Company for resale, which gas is produced in the Ivan Field of Webster and Bossier Parishes, Louisiana. The price of the gas is 9.87 cents per Mcf.

This matter is one that should be disposed of as promptly as possible under the applicable rules and regulations and to that end:

Take further notice that, pursuant to the authority contained in and subject to the jurisdiction conferred upon the Federal Power Commission by sections 7 and 15 of the Natural Gas Act, and the Commission's Rules of Practice and Procedure, a hearing will be held on September 8, 1955 at 9:30 a. m., e. d. s. t., in a Hearing Room of the Federal Power Commission, 441 G Street NW., Washington, D. C., concerning the matters involved in and the issues presented by such application: *Provided, however* That the Commission may, after a noncontested hearing, dispose of the proceedings pursuant to the provisions of section 1.30 (c) (1) or (c) (2) of the Commission's Rules of Practice and Procedure.

Protests or petitions to intervene may be filed with the Federal Power Commission, Washington 25, D. C., in accordance with the Rules of Practice and Procedure (18 CFR 1.8 or 1.10) on or before August 27, 1955. Failure of any party to appear at and participate in the hearing shall be construed as waiver of and concurrence in omission herein of the intermediate decision procedure in cases where a request therefor is made.

[SEAL] J. H. GUTRIDE,
Acting Secretary.

[F. R. Doc. 55-6566; Filed, Aug. 11, 1955; 8:47 a. m.]

[Docket No. G-8794]

UNITED EQUIPMENT CO. ET AL.

NOTICE OF APPLICATION AND DATE OF HEARING

AUGUST 8, 1955.

Take notice that United Equipment Company, George A. Butler, Robert S. Greenburg, Severin Knutson, Johnny Mitchell, Trustee, Martin Nadelman, Oil Drilling, Inc., J. S. Oshman, E. J. Pulaski, Louis Pulaski, Morris Rauch, Riddell Petroleum Corporation, Tennessee Production Company, W N. Zinn and Tennessee Gas Transmission Company, by and through their duly authorized agent, Christie, Mitchell and Mitchell Co. (hereinafter referred to as Applicant) whose address is 501 Bank of Commerce Building, Houston 2, Texas, filed on April 25, 1955, an application for a certificate of public convenience and necessity pursuant to section 7 of the Natural Gas Act, authorizing Applicant to render service as hereinafter described, subject to the jurisdiction of the Commission, all as more fully represented in the application which is on file with the Commission and open for public inspection.

Applicant proposes to sell natural gas to be produced from the Krezdorn Unit, Huffsmith Field, Harris County, Texas, to Tennessee Gas Transmission Company. The estimated rate of delivery will be 19,159 Mcf (at 14.65 p. s. i. a.) for the first month of delivery. The proposed initial price will be 13.69479 cents per Mcf (at 14.65 p. s. i. a.) Tennessee will transport and sell the gas, commingled with its other gas supplies, in interstate commerce.

This matter is one that should be disposed of as promptly as possible under the applicable rules and regulations and to that end:

Take further notice that, pursuant to the authority contained in and subject to the jurisdiction conferred upon the Federal Power Commission by sections 7 and 15 of the Natural Gas Act, and the Commission's Rules of Practice and Procedure, a hearing will be held on September 16, 1955, at 9:30 a. m., e. d. s. t., in a Hearing Room of the Federal Power Commission, 441 G Street NW., Washington, D. C., concerning the matters involved in and the issues presented by such application: *Provided, however* That the Commission may after a noncontested hearing, dispose of the proceedings pursuant to the provisions of section 1.30 (c) (1) or (c) (2) of the Commission's Rules of Practice and Procedure.

Protests or petitions to intervene may be filed with the Federal Power Commission, Washington 25, D. C., in accordance with the Rules of Practice and Procedure (18 CFR 1.8 or 1.10) on or before September 1, 1955. Failure of any party to appear at and participate in the hearing shall be construed as waiver of and concurrence in omission herein of the intermediate decision procedure in cases where a request therefor is made.

[SEAL] J. H. GUTRIDE,
Acting Secretary.

[F. R. Doc. 55-6567; Filed, Aug. 11, 1955; 8:47 a. m.]

[Docket No. G-9044]

HAVERHILL GAS CO.

NOTICE OF APPLICATION AND DATE OF HEARING

AUGUST 8, 1955.

Take notice that on June 16, 1955, Haverhill Gas Company (Applicant) filed an application, pursuant to section 7 (b) of the Natural Gas Act, for an order granting permission and approval to abandon sales and deliveries of natural gas to Allied New Hampshire Gas Company (Allied) for resale in Allied's Exeter (New Hampshire) Division.

Applicant proposes to abandon the service to Allied simultaneously with commencement of service to Allied by Tennessee Gas Transmission Company.

The application is on file with the Commission and open for public inspection.

This matter is one that should be disposed of as promptly as possible under the applicable rules and regulations, and to that end:

Take further notice that, pursuant to the authority contained in and subject to the jurisdiction conferred upon the Federal Power Commission by sections 7 and 15 of the Natural Gas Act, and the Commission's Rules of Practice and Procedure, a hearing will be held on September 15, 1955, at 9:30 a. m., e. d. s. t., in a Hearing Room of the Federal Power Commission, 441 G Street NW., Washington, D. C., concerning the matters involved and the issues presented by such application: *Provided, however,* That the Commission may, after a noncontested hearing, dispose of the proceedings pursuant to the provisions of section 1.30 (c) (1) or (c) (2) of the Commission's Rules of Practice and Procedure.

Protests or petitions to intervene may be filed with the Federal Power Commission, Washington 25, D. C., in accordance with the Rules of Practice and Procedure (18 CFR 1.8 or 1.10) on or before September 1, 1955. Failure of any party to appear at and participate in the hearing shall be construed as waiver of and concurrence in omission herein of the intermediate decision procedure in cases where a request therefor is made.

[SEAL] J. H. GUTRIDE,
Acting Secretary.

[F. R. Doc. 55-6568; Filed, Aug. 11, 1955; 8:47 a. m.]

[Docket No. G-9130]

BARNEY TRUMAN HEIRS LEASE

NOTICE OF APPLICATION AND DATE OF HEARING

AUGUST 8, 1955.

Take notice that Barney Truman Heirs Lease, C. W Beecher, Operator (Applicant) an individual whose address is Big Bend, West Virginia, filed on July 13, 1955, an application for a certificate of public convenience and necessity pursuant to section 7 of the Natural Gas Act, authorizing Applicant to render service as hereinafter described, subject to the jurisdiction of the Commission, all as more fully represented in the application which is on file with the Commission and open for public inspection.

Applicant produces natural gas from the Barney Truman Heirs Lease, on Daniels Run, Lee District, Calhoun County, West Virginia, which it proposes to sell to Hope Natural Gas Company at 20 cents per Mcf for transportation in interstate commerce for resale. The rate of delivery will be 300 Mcf per day.

This matter is one that should be disposed of as promptly as possible under the applicable rules and regulations and to that end:

Take further notice that, pursuant to the authority contained in and subject to the jurisdiction conferred upon the Federal Power Commission by sections 7 and 15 of the Natural Gas Act, and the Commission's Rules of Practice and Procedure, a hearing will be held on September 8, 1955, at 9:30 a. m., e. d. s. t., in a Hearing Room of the Federal Power Commission, 441 G Street NW., Washington, D. C., concerning the matters involved in and the issues presented by such application: *Provided, however* That the Commission may, after a noncontested hearing, dispose of the proceedings pursuant to the provisions of section 1.30 (c) (1) or (c) (2) of the Commission's Rules of Practice and Procedure.

Protests or petitions to intervene may be filed with the Federal Power Commission, Washington 25, D. C., in accordance with the Rules of Practice and Procedure (18 CFR 1.8 or 1.10) on or before August 26, 1955. Failure of any party to appear at and participate in the hearing shall be construed as waiver of and concurrence in omission herein of the intermediate decision procedure in cases where a request therefor is made.

[SEAL] J. H. GUTRIDE,
Acting Secretary.

[F. R. Doc. 55-6569; Filed, Aug. 11, 1955; 8:47 a. m.]

INTERSTATE COMMERCE COMMISSION

FOURTH SECTION APPLICATIONS FOR RELIEF

AUGUST 9, 1955.

Protests to the granting of an application must be prepared in accordance with Rule 40 of the General Rules of Practice (49 CFR 1.40) and filed within 15 days from the date of publication of this notice in the FEDERAL REGISTER.

LONG-AND-SHORT HAUL

FSA No. 30924: Cast iron pressure pipe in southern territory. Filed by R. E. Boyle, Jr., for interested rail carriers. Rates on cast iron pressure pipe, carloads, from specified points in Alabama, Florida, Georgia, North Carolina, Tennessee, and Virginia to specified points in Tennessee, Mississippi, and Virginia, also to Helena, Ark., Cairo and Metropolis, Ill., Evansville, Jeffersonville, and New Albany, Ind., and Cincinnati, Ohio.

Grounds for relief: Short-line distance scale, motor truck competition, and circuity.

Tariff: Supplement 57 to Agent Spaninger's I. C. C. 1374.

FSA No. 30925: Petroleum and products—Rogerslacy, Miss., to Illinois. Filed by R. E. Boyle, Jr., Agent, for interested rail carriers. Rates on petroleum and petroleum products, carloads, from Rogerslacy, Miss., to specified points in Illinois.

Grounds for relief: Commercial competition and circuity.

Tariff: Supplement 214 to Agent Spaninger's I. C. C. 1253.

FSA No. 30926: Alfalfa—Lamar, Colo., to Omaha, Nebr. Filed by W J. Prueter, Agent, for interested rail carriers. Rates on chopped or ground alfalfa (alfalfa meal) carloads from Lamar, Colo., to Omaha, Nebr.

Grounds for relief: Circuitous routes.

Tariff: Supplement 17 to Agent Prueter's I. C. C. A-3992.

FSA No. 30927: Steel sheet—Sault Ste. Marie, Mich., to Lansing, Mich. Filed by W. J. Prueter, Agent, for interested rail carriers. Rates on iron or steel sheet, strip, plate or bars, carloads, from Sault Ste. Marie, Mich., to Lansing, Mich.

Grounds for relief: Barge competition and circuity.

FSA No. 30928: Sand—Southwest to southern territory. Filed by F. C. Kratzmeir, Agent, for interested rail carriers. Rates on sand, noibn, ground or pulverized, carloads, from specified points in Arkansas, Missouri, Oklahoma and Texas to specified points in Alabama, Georgia, Kentucky, Mississippi, North Carolina, South Carolina, and Tennessee.

Grounds for relief: Short-line distance formula, market competition, and circuity.

Tariff: Supplement 28 to Agent Kratzmeir's I. C. C. 4135.

FSA No. 30929: Fertilizer and Materials—Middletown, Ohio, to the South. Filed by H. R. Hinsch, Agent, for interested rail carriers. Rates on fertilizer and fertilizer materials, carloads from Middletown, Ohio to specified points in Alabama, Arkansas (Helena), Florida, Georgia, Kentucky, Louisiana (east of the Mississippi River) Mississippi, North Carolina, South Carolina, Tennessee, and Virginia.

Grounds for relief: Short-line distance formula, market competition, and circuity.

Tariff: Supplement 18 to Agent Boin's I. C. C. A-984.

FSA No. 30930: Dense soda ash—From the East to Oklahoma. Filed by F. C. Kratzmeir, Agent, for interested rail carriers. Rates on dense soda ash, in bulk or in packages from specified points in Ohio, Michigan, New York and Virginia to Enid, Oklahoma City, and Ponca City, Okla.

Grounds for relief: Market competition and circuity.

Tariff: Supplement 89 to Agent Kratzmeir's I. C. C. 4109.

FSA No. 30931. Commodities from and to points in the Southwest. Filed by F. C. Kratzmeir, Agent, for interested rail carriers. Rates on commodities, various, in carloads from or to specified points in southwestern territory to or from specified points in southern and official territories.

Grounds for relief: Circuitous routes.

FSA No. 30932: Brick—Vale, Mo., to Kentucky and Tennessee. Filed by W. J. Prueter, Agent, for interested rail carriers. Rates on brick and related articles, carloads, from Vale, Mo., to specified points in Kentucky and Tennessee.

Grounds for relief: Market competition and circuity.

Tariff: Supplement 75 to Agent Prueter's I. C. C. A-3973.

By the Commission.

[SEAL] HAROLD D. McCOY,
Secretary.

[F. R. Doc. 55-6572; Filed, Aug. 11, 1955; 8:48 a. m.]

SECURITIES AND EXCHANGE COMMISSION

[File No. 24SF-2119]

SEARCHLIGHT URANIUM CORP.

ORDER TEMPORARILY DENYING EXEMPTION, STATEMENT OF REASONS THEREFOR, AND NOTICE OF OPPORTUNITY FOR HEARING

I. Searchlight Uranium Corporation, 2208 West Eighth Street, Los Angeles, California, having filed with the Commission on July 20, 1955, a Notification on Form 1-A, relating to a proposed public offering of 500,000 shares of 10 cent par value common stock at 10 cents per share, for the purpose of obtaining an exemption from the registration requirements of the Securities Act of 1933, as amended, pursuant to the provisions of section 3 (b) thereof and Regulation A promulgated thereunder; and

II. The Commission having been advised:

That an order was entered on June 30, 1953, in the United States District Court for the District of Nevada, permanently enjoining Homer C. Mills, president, director and promoter of Searchlight Uranium Corporation, and Searchlight Consolidated Mining & Milling Company, an affiliate of Searchlight Uranium Corporation, from further violations of the registration requirements of the Securities Act of 1933, as amended, in connection with the sale of securities of Searchlight Consolidated Mining & Milling Company; and

That on October 7, 1954, the United States District Court for the District of Nevada found Homer C. Mills guilty of

criminal contempt for having violated the terms of the aforesaid decree; and

It appearing necessary and appropriate in the public interest and for the protection of investors to deny the exemption under Regulation A under the Securities Act of 1933, as amended;

III. *It is ordered,* Pursuant to Rule 223 (a) of the General Rules and Regulations under the Securities Act of 1933, as amended, that the exemption under Regulation A be, and it hereby is, temporarily denied.

Notice is hereby given that any person having any interest in the matter may file with the Secretary of the Commission a written request for a hearing; that, within 20 days after receipt of such request, the Commission will, or at any time upon its own motion may, set the matter down for hearing at a place to be designated by the Commission for the purpose of determining whether this order of denial should be vacated or made permanent, without prejudice, however, to the consideration and presentation of additional matters at the hearing; and that notice of the time and place of said hearing will be promptly given by the Commission.

It is further ordered That this order and notice shall be served upon Searchlight Uranium Corporation, 2208 West Eighth Street, Los Angeles, California, and Homer C. Mills, Searchlight, Nevada, personally or by registered mail or by confirmed telegraphic notice and shall be published in the FEDERAL REGISTER.

By the Commission.

[SEAL] ORVAL L. DUBOIS,
Secretary.

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